(15)

No. 93-1001-CSX
Status: GRANTED

Title: Allied-Bruce Terminix Companies, Inc., and Terminix International Company, Petitioners
v.
G. Michael Dobson, et al.

Docketed:
December 22, 1993

Court: Supreme Court of Alabama

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Entry	Date	Note	Proceedings and Orders
1	Dec 22 1993	G	Petition for writ of certiorari filed.
3	Jan 21 1994		Order extending time to file response to petition until February 25, 1994.
4	Feb 25 1994		Brief of respondents G. Michael Dobson, et al. in opposition filed.
5	Feb 25 1994	G	Motion of Alabama Water and Sewer Institute, et al. for leave to file a brief as amici curiae filed.
6	Mar 2 1994		DISTRIBUTED. March 18, 1994 (Page 14)
7	Mar 4 1994	X	Reply brief of petitioners filed. VIDED.
8	Mar 21 1994		Motion of Alabama Water and Sewer Institute, et al. for leave to file a brief as amici curiae GRANTED.
9	Mar 21 1994		Petition GRANTED.
			**********
11	Apr 12 1994		Order extending time to file brief of petitioner on the merits until May 19, 1994.
12	May 18 1994	G	Motion of American Arbitration Association for leave to file a brief as amicus curiae filed.
13	May 18 1994		Brief amici curiae of Alabama Water and Wastewater Institute, et al. filed.
14	May 19 1994		Joint appendix filed.
15	May 19 1994		Brief of petitioners Allied-Bruce Terminix Companies, Inc., et al. filed.
16	May 19 1994		Brief amicus curiae of American Council of Life Insurance filed.
17	May 19 1994		Brief amici curiae of American Bankers Association, et al. filed.
19	May 26 1994		Order extending time to file brief of respondent on the merits until July 19, 1994.
20	Jun 6 1994		Motion of American Arbitration Association for leave to file a brief as amicus curiae GRANTED.
21	Jul 19 1994		Brief amici curiae of Alabama, et al. filed.
22	Jul 19 1994		Brief of respondents G. Michael Dobson, et al. filed.
24	Jul 19 1994		Brief amicus curiae of Southern Poverty Law Center filed.
25	Jul 20 1994		SET FOR ARGUMENT TUESDAY, OCTOBER 4, 1994. (1ST CASE).
23	Jul 21 1994		CIRCULATED.
26	Aug 2 1994		Record filed.
		*	Certified proceedings Supreme Court of Alabama and Circuit Court of Baldwin County (BOX)
27	Aug 19 1994	X	Reply brief of petitioners filed.

FILE COPY

No. 93-1001

IN THE
Supreme Court of the United States
OCTOBER TERM, 1993

Supreme Court, U.S.
FILED
DEC 22 1993
OFFICE OF THE CLERK

ALLIED-BRUCE TERMINIX COMPANIES, INC., and
TERMINIX INTERNATIONAL COMPANY,
Petitioners,

v.

G. MICHAEL DOBSON, WANDA C. DOBSON,
STEVEN GWIN and JAN GWIN,
Respondents.

Petition for a Writ of Certiorari to the Supreme Court of Alabama

PETITION FOR A WRIT OF CERTIORARI

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QUESTION PRESENTED

Section 2 of the Federal Arbitration Act, 9 U.S.C. § 2, makes an agreement to arbitrate enforceable, as a matter of federal law, provided that it is part of "a contract evidencing a transaction involving commerce." The question presented here is as follows:

Whether the Alabama Supreme Court correctly held—contrary to the view taken by most state and federal courts—that Section 2 is inapplicable to contracts otherwise involving interstate commerce if the parties did not "contemplate[] substantial interstate activity" at the time of the contract.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1993

No. ———

ALLIED-BRUCE TERMINIX COMPANIES, INC., and
TERMINIX INTERNATIONAL COMPANY,
Petitioners,

v.

G. MICHAEL DOBSON, WANDA C. DOBSON,
STEVEN GWIN and JAN GWIN,
Respondents.

Petition for a Writ of Certiorari to the Supreme Court of Alabama

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PETITION FOR A WRIT OF CERTIORARI

Petitioners respectfully request that a writ of certiorari issue to review the judgment of the Supreme Court of Alabama in this case.

OPINIONS BELOW

The opinion of the Supreme Court of Alabama is not yet reported. It is reprinted in the appendix to this petition at 1a-8a. The order of the circuit court is not reported. It is reprinted in the appendix to this petition at 9a.

JURISDICTION

The judgment of the Supreme Court of Alabama was entered on August 13, 1993. A timely petition for rehearing was denied on September 24, 1993. The jurisdiction of this Court is invoked pursuant to 28 U.S.C. § 1257(3).

STATUTORY PROVISIONS INVOLVED

Section 2 of the Federal Arbitration Act, 9 U.S.C. § 2, provides:

> **Validity, irrevocability, and enforcement of agreements to arbitrate**
>
> A written provision in any maritime transaction or a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction, or the refusal to perform the whole or any part thereof, or an agreement in writing to submit to arbitration an existing controversy arising out of such a contract, transaction, or refusal, shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract.

Section 1 of the Federal Arbitration Act, 9 U.S.C. § 1, provides in relevant part:

> **"Maritime transactions" and "commerce" defined; exceptions to operation of title**
>
> . . . "commerce", as herein defined, means commerce among the several States or with foreign nations, or in any Territory of the United States or in the District of Columbia, or between any such Territory and another, or between any such Territory and any State or foreign nation, or between the District of Columbia and any State or Territory or foreign nation, but nothing herein contained shall apply to contracts of employment of seamen, railroad employees, or any other class of workers engaged in foreign or interstate commerce.

STATEMENT

This case involves the construction of Section 2 of the Federal Arbitration Act (the "FAA" or "the Act"), 9 U.S.C. § 2.[1] Section 2, as a matter of federal substantive law, requires enforcement of arbitration agreements in any "contract evidencing a transaction involving commerce." Section 1 of the Act defines "commerce" to include "commerce among the several States" (9 U.S.C. § 1). The Alabama Supreme Court refused to enforce the arbitration agreement in this case, however, on the sole ground that, notwithstanding any *actual* nexus with interstate commerce, the parties had not "*contemplated* substantial interstate activity." Pet. App. 4a (quoting *Metro Indus. Painting Corp. v. Terminal Constr. Co.*, 287 F.2d 382, 387 (2d Cir.), *cert. denied*, 368 U.S. 817 (1961)) (Lumbard, J., concurring) (*Metro Indus.*).

The arbitration agreement was part of a contract between Steven and Jan Gwin and petitioners Allied-Bruce Terminix Companies, Inc. ("Terminix Service") and Terminix International Company ("Terminix International").[2] The Gwins, residents of Fairhope, Alabama, had previously agreed to a termite protection plan with a local company, but, upon its expiration, they decided "to go with a national company like Termin[i]x." C.R. 1346.[3] Terminix Service is an Arkansas company with offices in Florida, Georgia, Mississippi, Louisiana, Arkansas, Oklahoma, and Texas, as well as in Alabama. C.R. 272-73. Terminix International is a limited part-

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[1] All parties in the court below are reflected in the caption. The only corporate petitioner in this case—Allied-Bruce Terminix Cos., Inc.—has no parent company or subsidiaries.

[2] As we later discuss, the contract was subsequently transferred to respondents Michael and Wanda Dobson pursuant to a contract for purchase of the Gwins' home. *See* page 4 *infra*.

[3] "C.R." refers to the certified record in the Supreme Court of Alabama.

nership with its principal place of business in Memphis, Tennessee. C.R. 281.

The termite protection plan provided for services to be performed by Terminix Service. Terminix International, in turn, guaranteed the terms of the plan. C.R. 281. The contract embodying the plan expressly provided that "any controversy or claim between [the parties] arising out of or relating to the interpretation, performance or breach of any provision of this agreement *shall be settled exclusively by arbitration.*" C.R. 278-79, 280-85 (emphasis added).[4]

The termite protection plan was subsequently transferred to the Dobsons as part of their agreement to purchase the Gwins' home. C.R. 1664-65.[5] In addition, Terminix Service performed a visual inspection of the home, as called for in the sales agreement, to check for active infestation. C.R. 1500-01, 1652-53. Both the termite protection plan and the written report on the visual inspection were presented to the Dobsons at the closing of the sale. C.R. 1652-54, 1673-74.

[4] The full text of the arbitration provision is as follows:

> The Purchaser and Terminix agree that any controversy or claim between them arising out of or relating to the interpretation, performance or breach of any provision of this agreement shall be settled exclusively by arbitration. Such arbitration shall be conducted in accordance with the Commercial Arbitration Rules then in force of the American Arbitration Association before three arbitrators appointed by the American Arbitration Association. The arbitration award shall be final and binding on both parties. Judgment upon such arbitration award may be entered in any court having jurisdiction.

[5] The sales agreement included the following provision:

> SELLER IS TO FURNISH WRITTEN EVIDENCE from a bonded and licensed termite control company that a visual inspection by them indicates the dwelling is free from infestation by wood destroying insects and damage caused by currently active infestation. OLD DAMAGE IS NOT CONSIDERED. The current termite contract, if any, is to be transferred to Buyer at Buyer's expense.

Shortly after the closing, in the course of construction on the home, the Dobsons discovered termites. Although petitioners provided repairs and further treatment, in accordance with the terms of the termite protection plan,[6] the Dobsons were not satisfied. Rather than submit their complaints to arbitration, they brought suit against petitioners in Alabama Circuit Court, asserting claims that petitioners had breached their duties under the termite protection plan and that they had negligently performed the visual inspection. Pet. App. 2a.

Relying on the arbitration clause in the termite protection plan, petitioners sought to obtain a stay of the litigation and an order compelling arbitration. In so doing, petitioners specifically relied upon Section 2 of the Federal Arbitration Act. Petitioners argued that, as a matter of federal law, Section 2 required enforcement of voluntary arbitration agreements and that it preempted contrary state law. Without providing any reason for doing so, the Alabama Circuit Court, in a summary order, denied petitioners' motion. Pet. App. 9a.

The Alabama Supreme Court, likewise, refused to enforce the written arbitration agreement. The court acknowledged that Section 2 of the Act required enforcement of arbitration agreements as a matter of federal law, Pet. App. 2a-3a, but it held that Section 2 did not apply to this case because the required nexus with interstate commerce had not been met. In doing so, the court rejected petitioners' contention that the scope of Section 2—as reflected in the phrase "contract evidencing a transaction involving commerce"—should be broadly construed as "coextensive with [Congress'] commerce power." Pet. App. 3a. Rather, the court opted to apply a more restrictive standard, stating that " '[t]he significant question,

[6] Much of the material and equipment used to treat the home—including the chemical used to eliminate and prevent termites—was purchased outside of Alabama and brought into Alabama for use on the home. C.R. 272-73.

therefore [in determining whether a contract evidences a transaction involving commerce] is not whether, in carrying out the terms of the contract, the parties *did* cross state lines, but whether, at the time they entered into it and accepted the arbitration clause, they *contemplated* substantial interstate activity.'" Pet. App. 4a (quoting *Metro Indus.*, 287 U.S. at 387 (Lumbard, J., concurring)). Applying that test, and finding insufficient evidence that "the parties contemplated substantial interstate activity when they entered the termite bond," Pet. App. 5a, the court determined that federal law did not apply. Pursuant to state policy against enforcement of pre-dispute arbitration agreements, it thus declined to enforce the agreement.

REASONS FOR GRANTING THE WRIT

This case involves an important issue regarding the scope of Section 2 of the Federal Arbitration Act. Section 2—which embodies a "liberal federal policy favoring arbitration agreements" (*Moses H. Cone Memorial Hosp. v. Mercury Constr. Co.*, 460 U.S. 1, 24 (1983) (*Moses H. Cone*))—applies by its express terms to any "contract evidencing a transaction involving commerce." Although most federal and state courts have read this phrase broadly, in keeping with the federal policy, *see, e.g., Foster v. Turley*, 808 F.2d 38 (10th Cir. 1986), the Alabama Supreme Court has taken quite the opposite course, holding that Section 2 applies, not when a transaction *in fact* involves interstate commerce, but only when the parties "*contemplated* substantial interstate activity." Pet. App. 4a (quoting *Metro Indus.*, 287 U.S. at 387 (Lumbard, J., concurring)). In explaining its adoption of this test, moreover, the Alabama court has candidly admitted that its narrow construction "better promotes our strong public policy *against* the use of predispute arbitration agreements." *Lopez v. Home Buyers Warranty Corp.*, No. 1920330, 1993 Ala. LEXIS 818, at *6 n.2 (Aug. 20, 1993) (emphasis added).

This hostile reading of Section 2 is flatly contrary to the principle that "questions of arbitrability must be addressed with a healthy regard for the federal policy favoring arbitration." *Moses H. Cone*, 460 U.S. at 24. Rather than follow *federal* policy, the Alabama court has adopted a narrow view of federal law that reflects *state* policies against arbitration. Moreover, putting aside questions of policy, its construction of Section 2 is almost certainly wrong. As this Court has recognized, Section 2 was enacted pursuant to powers conferred by the Commerce Clause, *see Southland Corp. v. Keating*, 465 U.S. 1 (1984), and nothing in the language of Section 2—or Section 1, which contains a broad definition of "commerce"—gives any hint that Congress meant to exercise only a fraction of that power. Thus, so long as a transaction in fact involves interstate commerce, it seems clear that Congress intended to make agreements to arbitrate as enforceable as any other contract. *See Gilmer v. Interstate/Johnson Lane Corp.*, 111 S. Ct. 1647, 1651 (1991).

The decision below also sharpens an unwarranted division among state and federal courts on this issue. As we have noted, most federal and state courts addressing the question have read Section 2 broadly to reach any transaction that has an actual nexus with interstate commerce. *See, e.g., Foster v. Turley; Snyder v. Smith*, 736 F.2d 409, 417-18 (7th Cir.), *cert. denied*, 469 U.S. 1037 (1984); *Del E. Webb Constr. v. Richardson Hosp. Auth.*, 823 F.2d 145, 147 (5th Cir. 1987). Several state courts, however, have applied the same narrow test as the Alabama courts, enforcing arbitration agreements only when the parties "contemplated" that the particular transaction would involve interstate commerce. *See, e.g., Burke County Pub. Schools Bd. of Educ. v. Shaver Partnership*, 279 S.E.2d 816 (N.C. 1981); *Pathman Constr. Co. v. Knox County Hosp. Ass'n*, 326 N.E.2d 844 (Ind. 1975). The unequivocal commitment of the Alabama courts to the latter test—reflected in a series of recent cases, including this one—makes clear that this conflict will not

end of its own accord. *See, e.g., Jackson v. The Terminix International Co. Limited Partnership*, No. 1911842, 1993 Ala. LEXIS 803 (Aug. 13, 1993); *Lopez v. Home Buyers Warranty Corp.*; *Henderson v. Superior Ins. Co.*, No. 1920541, 1993 Ala. LEXIS 812 (Aug. 20, 1993); *Ex parte Jones*, No. 1920249, 1993 Ala. LEXIS 662 (July 16, 1993). Without guidance from this Court, therefore, the application of Section 2 will needlessly vary from jurisdiction to jurisdiction, directly frustrating Congress' intention to establish uniform federal law making arbitration agreements "valid, irrevocable, and enforceable" in all state and federal courts. *See Southland Corp. v. Keating*, 465 U.S. at 15.

I. THE DECISION BELOW IS BASED UPON A MISREADING OF SECTION 2 AND CONTRAVENES FEDERAL POLICY FAVORING ENFORCEABILITY OF ARBITRATION AGREEMENTS.

It is well-established that Section 2 of the Federal Arbitration Act "is a congressional declaration of a liberal federal policy favoring arbitration agreements, notwithstanding any state substantive or procedural policies to the contrary." *Moses H. Cone*, 460 U.S. at 24; *see Perry v. Thomas*, 482 U.S. 483, 489 (1987). As this Court has recognized, the purpose of Section 2 "was to reverse the longstanding judicial hostility to arbitration agreements that had existed at English common law and had been adopted by American courts, and to place arbitration agreements upon the same footing as other contracts." *Gilmer v. Interstate/Johnson Lane Corp.*, 111 S. Ct. at 1651. Drawing upon its "comprehensive powers" under the Commerce Clause, *Southland Corp. v. Keating*, 465 U.S. at 15, Congress sought to "create a body of federal substantive law of arbitrability, applicable to any arbitration agreement within the coverage of the Act." *Moses H. Cone*, 460 U.S. at 24. Within the fields that it encompasses, therefore, Section 2 requires that courts "rigorously enforce agreements to arbitrate." *Dean Witter Reynolds, Inc. v. Byrd*, 470 U.S. 213, 221 (1985); *see Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 626 (1985).

Although this Court has not precisely defined the phrase at issue here—*i.e.*, "contracts evidencing transactions involving commerce"—it has long viewed the term as having broad reach. In *Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, 388 U.S. 395 (1967), for example, the Court declined to limit application of Section 2 to "contracts between merchants for the interstate shipment of goods," *id.* at 401 n.7, finding no basis for that in either the language or history of the Act. As part of its analysis, the Court specifically noted language in a relevant House Report stating that " '[t]he control over interstate commerce [one of the bases for the legislation] reaches not only the actual physical interstate shipment of goods *but also contracts relating to interstate commerce.*' " *Id.* (quoting H.R. Rep. No. 96, 68th Cong., 1st Sess. 1 (1924)) (emphasis added).[7] More recently, the Court, again without actually deciding the question, declared that "the Federal Arbitration Act . . . embodies Congress' intent to provide for the enforcement of arbitration agreements *within the full reach of the Commerce Clause.*" *Perry v. Thomas*, 482 U.S. at 490 (emphasis added).

The decision below, however, takes a very different view. Relying on a standard fashioned more than three decades ago—long before this Court made clear the full extent of the federal policy favoring arbitration—the Alabama courts have imposed a requirement that the parties regard their dealings as involving interstate commerce, rather than simply looking to whether the dealings in fact

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[7] Although the Court, in *Bernhardt v. Polygraphic Co.*, 350 U.S. 198 (1956), held that an employment contract did not evidence a transaction involving commerce, it did so only after finding "no showing that [the employee] while performing his duties under the employment contract was working 'in' commerce, was producing goods for commerce, or was engaging in activity that affected commerce, within the meaning of our decisions." *Id.* at 200-01.

do so. Thus, even though (as in this case) a transaction may involve parties in different states and the movement of goods across state lines—and thus is unquestionably within the reach of Congress' powers under the Commerce Clause—the Alabama courts refuse to apply federal law, unless the parties also "*contemplated* substantial interstate activity." Pet. App. 7a (emphasis added). This limitation on federal law, not coincidentally, allows for greater application of state policies, particularly those (as in Alabama) that disfavor enforcement of agreements to arbitrate.

This reading is directly at odds with both the language and the policies of the Act. The term "transaction involving commerce," on its face, plainly calls for an inquiry into actual interstate activity, rather than the expectations of the parties, and the broad definition of "commerce" in Section 1 likewise points toward application of an objective standard (*i.e.*, whether the transaction involves "commerce among the several States"). While the contract containing the arbitration agreement must "evidence" the transaction involving commerce, as Judge Lumbard noted in his concurring opinion in *Metro Indus.* (287 F.2d at 386), that language, naturally read, means only that the contract must be evidence of the *transaction*, not its interstate nature. Thus, provided that the transaction actually involves interstate commerce, and provided that the contract is evidence of the transaction, Section 2 makes the agreement to arbitrate enforceable, regardless of whether the parties openly make reference to (or otherwise "contemplate") the interstate elements in their contract.

Quite apart from the plain language of the statute, it makes little sense to think that Congress would have favored a narrow test keyed to the subjective "contemplation-of-the-parties." In recent years, for example, this Court has repeatedly rejected arguments that Section 2 is inapplicable to claims arising under federal statutes.

See, e.g., Gilmer v. Interstate/Johnson Lane Corp.; *Perry v. Thomas*; *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*; *Dean Witter Reynolds, Inc. v. Byrd.* Noting that Congress intended to promote enforcement of agreements to arbitrate, *see, e.g., Mitsubishi Motors*, 473 U.S. at 627, the Court has observed that "the [Federal Arbitration] Act itself provides no basis for disfavoring agreements to arbitrate statutory claims by skewing the otherwise hospitable inquiry into arbitrability." *Id.* By the same token, the Act gives no basis for thinking that Congress would want to limit the field of its application solely on the basis of what the parties understood about the interstate nature of their transaction.

The "contemplation-of-the-parties" test, at bottom, seems to rest upon a confusion of two necessary but distinct elements under Section 2: first, a subjective agreement to arbitrate; and, second, an objective nexus to interstate commerce. The first requirement establishes that there is, in fact, a voluntary agreement to enforce pursuant to Section 2, and the second requirement establishes that the transaction is within the field defined by Congress and within reach of the powers allotted to Congress under the Constitution. It distorts the Act, however, to combine the two requirements into a third requirement: that the parties must "contemplate" the elements necessary to bring the transaction within the terms of the statute. Whether or not that is the case, the parties have *agreed to arbitrate* their disputes, and the sole remaining inquiry is whether Congress, having exercised its power over interstate commerce, has made that agreement enforceable. The contemplation of the parties has nothing logically to do with that question.[8]

[8] There is nothing inherently inequitable about a general rule requiring parties to a contract to abide by their agreement to arbitrate. If a particular agreement resulted from fraud, or any other behavior that would be grounds "for the revocation of any contract" (9 U.S.C. § 2), then federal policy does not require that it be enforced. *Gilmer*, 111 S. Ct. at 1655-56; *Mitsubishi Motors*, 473 U.S. at 627.

The construction given Section 2 by the Alabama courts is almost certainly tied to its "strong public policy against the use of predispute arbitration agreements." *Lopez v. Home Buyers Warranty Corp.*, No. 1920330, 1993 Ala. LEXIS 818, at *6 n.2. That sort of hostility towards arbitration agreements, of course, is precisely what Section 2 was meant to override. *See, e.g., Gilmer*, 111 S. Ct. at 1651. But, whatever the motive, a grudging reading of the Act should not be allowed to stand. If state courts may define Section 2 narrowly, and thus avoid preemption of contrary state policies, the federal policy favoring enforcement of arbitration agreements will be severely undercut. *See Securities Indus. Ass'n v. Connolly*, 883 F.2d 1114, 1119 (1st Cir. 1989), *cert. denied*, 495 U.S. 956 (1990) ("courts must be on guard for artifices in which the ancient suspicion of arbitration might reappear"). For that reason alone, review by this Court is appropriate.

II. THE STATE AND FEDERAL COURTS HAVE ADOPTED DIFFERENT CONSTRUCTIONS OF SECTION 2 CONTRARY TO THE NEED FOR UNIFORM FEDERAL LAW REGARDING ARBITRATION AGREEMENTS.

The issue presented here also has divided state and federal courts. Most courts addressing the issue have held that the phrase "contract evidencing a transaction involving commerce" must be broadly construed, expressly relying on the federal policy favoring enforcement of arbitration agreements. *See, e.g., Snyder v. Smith*, 736 F.2d at 417-18; *Societe Generale de Surveillance, S.A. v. Raytheon European Management & Sys. Co.*, 643 F.2d 863, 867 (1st Cir. 1981); *Foster v. Turley*, 808 F.2d at 40; *Del E. Webb Constr. v. Richardson Hosp. Auth.*, 823 F.2d at 147; *Woermann Constr. Co. v. Southwestern Bell Tel. Co.*, 846 S.W.2d 790, 792 (Mo. Ct. App. 1993). Thus, in the Tenth Circuit, "[t]he requirement that the underlying transaction involve commerce is to be broadly construed *so as to be coextensive with congressional power to regulate under the Commerce Clause.*" *Foster v. Turley*, 808 F.2d at 40 (emphasis added). In the Fifth Circuit, Section 2 applies to any contracts that "*relate to* interstate commerce, a standard that implements the strong federal policy favoring arbitration." *Del E. Webb*, 823 F.2d at 148. Similarly, the First Circuit has declared that "the term 'commerce' in this provision of the Act refers to interstate or foreign commerce and is to be broadly construed." *Societe Generale*, 643 F.2d at 867. *See also C.P. Robinson Constr. Co. v. National Corp. for Housing Partnerships*, 375 F. Supp. 446, 450 (M.D.N.C. 1974) ("the question as to whether the contract evidences a transaction in commerce must be determined by application of the statutory definition of 'commerce' to the objective facts of the case").[9]

Other courts—primarily state courts—have chosen to follow the test applied below. *See Burke County Pub. Schools Bd. of Educ. v. Shaver Partnership; Pathman Constr. Co. v. Knox County Hosp. Ass'n; R.J. Palmer Constr. Co. v. Wichita Band Instrument Co.*, 642 P.2d 127 (Kan. Ct. App. 1982); *Loche v. Dean Witter Reynolds, Inc.*, 526 N.E.2d 1296 (Mass. App. Ct. 1988); *Lacheney v. Profitkey Int'l, Inc.*, 818 F. Supp. 922 (E.D. Va. 1993). This test, fashioned by Judge Lumbard some thirty years ago, holds that the proper inquiry under Section 2 "is not whether, in carrying out the terms of the contract, the parties *did* cross state lines, but whether, at the time they entered into it and accepted the arbitration clause, they *contemplated* substantial interstate activ-

[9] We note that the Alabama courts, at one time, applied a similar standard, holding that Section 2 applied as long as the transaction had the "slightest nexus" with interstate commerce. *See Ex parte Costa & Head (Atrium), Ltd.*, 486 So. 2d 1272, 1275 (Ala. 1986). Subsequently, in *Ex parte Warren*, 548 So. 2d 157 (Ala.), *cert. denied*, 493 U.S. 998 (1989), the Alabama Supreme Court utilized the "contemplation-of-the-parties" test but did not overrule *Costa & Head*. The use of the "slightest nexus" test was then explicitly disavowed this year in *Ex parte Jones*, *supra*.

ity." *Metro Indus.*, 287 F.2d at 387. Contrary to the approach in most jurisdictions, therefore, courts following the Lumbard test expand or contract federal law depending "not on what in fact happened, but on what was in the contemplation of the parties as manifested in their written agreement." *Id.*

This lack of uniformity cannot be squared with the objectives of the Act. Although the different tests will sometimes lead to the same conclusion—that is, facts about a particular transaction may satisfy both tests or neither—often they will not. This Court has said, in holding that Section 2 applies in state as well as federal courts: "We are unwilling to attribute to Congress the intent, in drawing on the comprehensive powers of the Commerce Clause, to create a right to enforce an arbitration contract and yet make the right dependent for its enforcement on the particular forum in which it is asserted." *Southland Corp. v. Keating*, 465 U.S. at 15. Yet, as long as the language of Section 2 means one thing in some courts, and something quite different in other courts, the right to enforce arbitration contracts will continue to depend "on the particular forum in which it is asserted."

This judicial disagreement also goes to the most basic, and delicate, of questions under the Act: whether federal or state law governs the enforceability of an arbitration agreement. This is not a question to which there can be two correct answers. If the majority of state and federal courts is correct, and Section 2 has a broad scope reflecting Congress' powers under the Commerce Clause, then the Alabama courts, and other courts following the "contemplation-of-the-parties" standard, are wrongly applying state law to arbitration agreements that federal law makes enforceable. If the narrower reading is correct, however, then judges in numerous federal and state courts are improperly overriding state law whenever a transaction objectively involves interstate commerce but the parties did

not so contemplate in their agreement. A ruling from this Court would put all courts on the same footing.

Finally, the uncertainty raised by different tests creates obstacles to the conduct of interstate business. Under federal law, businesses engaged in an interstate transaction should be able to rely on an agreement to arbitrate disputes between the contracting parties. But, as matters now stand, the ability to rely on an arbitration agreement may depend on whether the court hearing a lawsuit (brought in violation of the agreement to arbitrate) takes a broad or narrow view of the nexus requirement of Section 2. Indeed, given that interstate transactions by definition involve more than one state, it frequently will be difficult, if not impossible, for businesses to know, at the time that they negotiate contracts, whether agreements to arbitrate are binding or not. This uncertainty is directly contrary to Congress' goal to make arbitration agreements "valid, irrevocable, and enforceable," as a matter of federal law. 9 U.S.C. § 2.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,

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APPENDICES

APPENDIX A

SUPREME COURT OF ALABAMA

SPECIAL TERM, 1993

1920473

ALLIED-BRUCE TERMINIX COMPANIES, INC., *et al.*

v.

G. MICHAEL DOBSON, WANDA C. DOBSON, STEVEN GWIN, and JAN GWIN

Appeal from Baldwin Circuit Court
(CV-91-796)

ALMON, JUSTICE.

The defendants, Allied-Bruce Terminix Companies, Inc. ("Terminix Service"), and Terminix International Company ("Terminix International") appeal from an order of the trial court denying their motion to compel arbitration of the tort and breach of contract claims filed against them by Michael Dobson, Wanda Dobson, Steven Gwin, and Jan Gwin. The issue for our review is whether the arbitration clause contained in a termite bond is enforceable under the Federal Arbitration Act, 9 U.S.C. § 1 et seq. ("FAA").

In August 1987, Steven Gwin allowed the termite bond on his house in Fairhope, Alabama, to expire, and he

purchased a replacement bond from Terminix Service. Terminix Service is an Arkansas corporation that does business in several states, including Alabama, Arkansas, Florida, Georgia, Mississippi, Louisiana, Oklahoma, and Texas. The bond was guaranteed by Terminix International, a limited partnership that has its principal place of business in Memphis, Tennessee.

In 1991, Steven and Jan Gwin agreed to sell the house to Michael and Wanda Dobson. The sales contract required the Gwins to provide written evidence from a licensed pest control company that the company had performed a visual inspection of the house and had observed no active infestation of termites or damage from active infestation. The contract also required that the termite bond be transferred to the Dobsons at the closing of the sale. Because of the existing bond on the house, Terminix Service agreed to perform the inspection and to issue the required statement. At the closing, the Gwins furnished Dobson with a standard Veterans' Administration ("VA") form; the V.A. form provided that Terminix Service had observed no visible evidence of active infestation during the inspection.

The Dobsons later discovered termite damage to the house, and they brought an action against the Gwins, alleging fraud, and against Terminix Service and Terminix International, alleging fraud in connection with the representations in the V.A. form, and alleging breach of contract. The Gwins cross-claimed against Terminix Service and Terminix International. Terminix Service and Terminix International moved to stay the proceedings and to compel the Dobsons and the Gwins to submit their claims to arbitration pursuant to an arbitration clause in the bond. The trial court denied this motion, and the defendants appeal.

Predispute arbitration agreements are unenforceable under Alabama law. Ala. Code 1975, § 8-1-41. However, if an arbitration agreement is voluntarily entered into and

is contained in a contract that involves interstate commerce, then the FAA preempts state law and renders the agreement enforceable. *A.G. Edwards & Sons, Inc. v. Syvrud,* 597 So. 2d 197 (Ala. 1992). The Terminix companies contend that, because the United States Supreme Court has held in *Southland Corp. v. Keating,* 465 U.S. 1, 104 S.Ct. 852, 79 L.Ed.2d 1 (1984), that Congress's regulatory power under the FAA is co-extensive with its commerce power, this Court should apply the "slightest nexus" standard first enunciated in *Ex parte Costa & Head (Atrium), Ltd.,* 486 So. 2d 1272 (Ala. 1986), to this situation. This standard provides that if the contract in question has the slightest nexus with interstate commerce, the FAA will apply. *Costa & Head*; *Ex parte Brice Building Co.,* 607 So. 2d 132 (Ala. 1992). Terminix Service and Terminix International argue that, because they are out-of-state entities, and because some of the materials used in fulfilling their duties imposed by the termite bond were brought into Alabama from out-of-state, the bond has at least a "slight nexus" with interstate commerce.

We need not address this argument, however, in light of this Court's decision in *Ex parte Jones,* [Ms. 1920249, July 16, 1993] —— So. 2d —— (Ala. 1993).[1] In *Jones,* we explicitly rejected the *Costa & Head* "slightest nexus" standard in favor of the standard enunciated in *Ex parte Warren,* 548 So. 2d 157 (Ala. 1989), cert. denied, 493 U.S. 998, 110 S.Ct. 554, 107 L.Ed.2d 550 (1989). We held:

> "To resolve any inconsistency or confusion generated by the existence of two different standards, and determining, as we now do, that *Warren* represents a more reasoned approach than the *Costa* standard, we overrule any case inconsistent with *Warren,* to

[1] See also *Continental Grain Co. v. Beasley,* [Ms. 1920241, July 16, 1993] —— So. 2d —— (Ala. 1993).

the extent that it states a different standard for determining the involvement of interstate commerce."

—— So. 2d at ——. The *Warren* standard, which was invoked in *Warren* to cover only the "narrow" circumstances in which Alabama residents had purchased an automobile for consumer purposes from an in-state dealership, was first set forth by Judge Lombard in a special concurrence in *Metro Industrial Painting Corp. v. Terminal Constr. Co.*, 287 F.2d 382 (2d Cir.), cert. denied, 368 U.S. 817, 82 S.Ct. 31, 7 L.Ed.2d 24 (1961):

> "The significant question, therefore [in determining whether a contract evidences a transaction involving commerce], is not whether, in carrying out the terms of the contract, the parties *did* cross state lines, but whether, at the time they entered into it and accepted the arbitration clause, they *contemplated* substantial interstate activity. Cogent evidence regarding their state of mind at the time would be the terms of the contract, and if it, on its face, evidences interstate traffic . . . the contract should come within § 2 [of the FAA.] In addition, evidence as to how the parties expected the contract to be performed and how it was performed is relevant to whether substantial interstate activity was contemplated."

287 F.2d at 387 (emphasis in original).

Terminix Service and Terminix International argue that the bond involves interstate commerce even under the more restrictive *Warren* standard. In addition to the evidence cited above in support of their *Costa & Head* argument, the Terminix companies cite the following in support of their contention that at the time they entered into the contract the parties "contemplated substanial interstate activity": Steven Gwin's testimony that he allowed his bond with a local pest control company to expire so that he could "go with a national company like Terminix"; the fact that the bond instrument showed on its face that it was executed in Memphis, Tennessee; and the fact that the bond contained a statement that it was subject to federal regulation.

A brief survey of cases from other jurisdictions that have applied the standard will be useful in determining whether the parties contemplated substantial interstate activity when they entered the termite bond.

Several cases applying the *Warren* standard involve contracts for the construction of large projects. In *Burke County Public Schools Board of Educ. v. Shaver Partnership*, 303 N.C. 408, 279 S.E.2d 816 (1981), the North Carolina Supreme Court held that a contract between a North Carolina school board and an Indiana architectural firm for the construction of school buildings did involve interstate commerce so as to be covered by the FAA. In so holding, the Court stated:

> "We do not mean to suggest that where the contracting parties are merely located in different states or where other facts tending only to show diversity of citizenship are present, the contract must necessarily be found to contemplate substantial interstate activity so as to trigger the act's applicability. Where, however, performance of the contract necessarily involves, so that the parties must have contemplated, substantial interstate activity, the contract evidences a transaction involving commerce within the meaning of the [FAA]."

303 N.C. at 418, 279 S.E.2d at 822. The Court then held that the following evidence established that when they entered into the contract the parties contemplated substantial interstate activity: certain contractual provisions called for the Indiana firm to come to the North Carolina building site for various reasons; accounting records on the project were maintained in Kansas; the Indiana firm dealt with suppliers from across the country in performing its contractual duties; and certain design work was performed by a Michigan firm. See also *G.D. Searle*

& Co. v. Metric Constructors, Inc., 572 F.Supp. 836 (N.D. Ga. 1983); *Dimambro-Northend Assocs. v. Blanck-Alvarez, Inc.*, 251 Ga. 704, 309 S.E.2d 364 (1983); *University Casework Systems, Inc. v. Bahre*, 172 Ind. App. 624, 362 N.E.2d 155 (1977).

Some courts have also held the FAA applicable to contracts for the construction of smaller projects. In *R.J. Palmer Constr. Co. v. Wichita Band Instrument Co.*, 7 Kan. App.2d 363, 642 P.2d 127 (1982), the Kansas Court of Appeals held that the FAA applied to a contract for the construction of a music store. The Court held that because the store was to be built out of California redwood, the parties knew that the contract would involve interstate activity.

A smaller number of cases applying the *Warren* standard involve personal service contracts. For example, in *Bennish v. North Carolina Dance Theatre, Inc.*, 108 N.C. App. 42, 422 S.E.2d 335 (1992), the North Carolina Court of Appeals held that a dancer and his employer contemplated substantial interstate activity when they entered the contract, because the contract provided guidelines on air travel and the employer introduced evidence that the dancer toured outside of North Carolina for a substantial amount of the contract period. See also *Erving v. Virginia Squires Basketball Club*, 468 F.2d 1064 (2d Cir. 1972).

We conclude that the evidence adduced by the Terminix companies does not establish that the parties contemplated substantial interstate activity when they entered the termite bond. Initially, we note that we have held in *A.J. Taft Coal Co. v. Randolph*, 602 So. 2d 395 (Ala. 1992)—which was decided under the *Costa & Head* standard—that it is insufficient for the purposes of invoking the FAA merely to show that one or more of the parties to the contract is located in another state. Therefore, under the more restrictive *Warren* standard, the fact

that the bond stated that it was executed in Tennessee is not determinative. Terminix's second piece of evidence, that the bond stated that it was subject to federal regulation, is based on the following paragraph in the bond:

> "Change in Law. Terminix performs its services in accordance with the requirements of federal, state, and local law. In the event of a change in existing law as it pertains to the services promised herein, Terminix reserves the right to revise the annual extension charge or terminate this agreement."

A bare statement in the bond that Terminix adheres to the requirements of any federal law applicable to its services simply does not show that the parties contemplated that the bond would involve substantial interstate activity in any way. Unlike the contractual provisions in *Bennish*, *supra*, it certainly does not put the plaintiffs on notice of the likelihood of substantial interstate activity. Moreover, Gwin's statement that he wished to go with a "national" company is not evidence that he contemplated anything; that statement merely reflects a desire on Gwin's part to receive the added security that many people associate with a large, national company. Finally, the *performance* of the bond obligations did not involve interstate commerce to such a degree that the parties upon entering the contract must have contemplated substantial interstate activity. Although some materials used in fulfilling the bond obligations may have come from out-of-state suppliers, this is not analogous to those situations—such as the aforementioned construction contracts involving large projects, or contracts for personal services—where the interstate activity involved in the performance of the contract is so great that it cannot reasonably be said that the parties failed to contemplate substantial interstate activity when they entered into the contract. See *Terminix Int'l Co. v. Jackson*, [Ms. 1911842, Aug. 13, 1993] —— So. 2d ——(Ala. 1993).

For the foregoing reasons, the judgment of the trial court is due to be affirmed.

AFFIRMED.

Houston, Steagall, and Ingram, JJ., concur.

Kennedy, J., concurs in the result.

APPENDIX B

THE CIRCUIT COURT OF BALDWIN COUNTY

Case No. CV 91-796

G. MICHAEL DOBSON, *et al.*

vs.

THE TERMINIX INTERNATIONAL CO., *et al.*

Motion for order compelling arbitration and for order of stay pending arbitration is denied.

/s/ James H. Reid
Judge

APPENDIX C

IN THE SUPREME COURT OF ALABAMA
SEPTEMBER 24, 1993

1920473

ALLIED-BRUCE TERMINIX COMPANIES, INC., *et al.*

v.

G. MICHAEL DOBSON, WANDA C. DOBSON,
STEVEN GWIN, and JAN GWIN,

(Baldwin: CV-91-796)

NOTICE

The application for rehearing filed in this cause is overruled. No opinion written on rehearing.

ALMON J.—Houston, Steagall, Kennedy and Ingram, JJ., concur.

Supreme Court, U.S.
FILED
FEB 25 1994
OFFICE OF THE CLERK

No. 93-1001

In The

Supreme Court of the United States

October Term, 1993

ALLIED-BRUCE TERMINIX COMPANIES, INC., and TERMINIX INTERNATIONAL COMPANY,

Petitioners,

v.

G. MICHAEL DOBSON, WANDA C. DOBSON, STEVEN GWIN and JAN GWIN,

Respondents.

On Petition For A Writ Of Certiorari To The Supreme Court Of Alabama

BRIEF IN OPPOSITION TO PETITION FOR A WRIT OF CERTIORARI

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QUESTION PRESENTED

Whether the contract at issue here – a "termite protection plan" to provide pest control services in Alabama to an Alabama homeowner by a company operating locally in Alabama – is, under the particular facts of this case, a "contract evidencing a transaction involving commerce" within the meaning of Section 2 of the Federal Arbitration Act.

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STATEMENT OF THE CASE

Petitioners' Statement of the Case is substantially correct except in one respect. Petitioners assert, at page 5 of the Brief, that

> [r]ather than submit their complaints to arbitration, [Dobson] brought suit against petitioners in Alabama Circuit Court, asserting claims that petitioners had breached their duties under the termite protection plan and that they had negligently performed the visual inspection.

Actually, the Complaint, as initially filed by Dobson, contained claims against Terminix Service and Terminix International Company LP (hereinafter referred to as "Terminix International") only for misrepresentation based on a report or clearance letter furnished to Dobson following a pre-closing inspection of the house by Terminix Service; and for negligence or wantonness in connection with the inspection itself. (See Complaint at R. 1-5) No breach of contract claims were asserted by Dobson at that time. Neither Terminix Service nor Terminix International demanded arbitration at that time, but filed Answers to the Complaint. (R. 27-37 and 38-48) The litigation process was substantially invoked for a period of more than eight months when, on June 25, 1992, Dobson filed an Amended Complaint which, among other things, stated a claim against both Terminix Service and Terminix International for breach of contract. (See First Amended Complaint, R. 182-186) On August 14, 1992, both Terminix Defendants, for the first time, sought arbitration (R. 286-300), which request was denied by the Circuit Court of Baldwin County, Alabama, without statement of reasons. Dobson raised an issue on appeal to the Supreme

Court of Alabama concerning the proper scope of the arbitration clause, if valid at all, which issue was not reached by that Court. If the arbitration clause is binding on Dobson and if the tort claims are determined to be within the scope of that clause, then additional issues would be raised by Dobson concerning the timeliness of the request for arbitration, as to the tort claims.

REASONS FOR DENYING THE WRIT

The Petition should be denied because it does not raise issues that warrant review by this Court. The question presented here is whether the contract at issue in this case, a homeowner "termite protection plan," can be regarded as a "transaction involving commerce" under Section 2 of the Federal Arbitration Act.

In the discussion which follows, we first explain why such a local contract cannot be regarded as "involving commerce" under any test.

We then explain why Petitioners are simply wrong in suggesting that there exists a division of authority among state and federal courts as to the test to be applied in resolving this issue. An examination of the cases cited by Petitioners as evidence of that division of authority are not persuasive. While the rationale may vary somewhat from case to case, the result, in cases based on similar facts, is remarkably similar.

Nor are Petitioners correct in asserting that the decision below conflicts with the interpretation of Section 2 by this Court, particularly in *Perry v. Thomas*, 482 U.S. 483

(1987). We do not believe that *Perry* speaks to the issue of which transactions involve interstate commerce. Rather, we would suggest that *Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, 388 U.S. 395 (1967), and *Bernhardt v. Polygraphic Co. of America, Inc.*, 350 U.S. 198 (1956), are the relevant authorities on that issue and that the decision below is not in conflict with either.

I. THE CONTRACT AT ISSUE IN THIS CASE DOES NOT EVIDENCE A TRANSACTION INVOLVING INTERSTATE COMMERCE UNDER ANY TEST.

This case arises out of the purchase of a residential dwelling in Alabama by the Respondents, Dobson, residents of Alabama, from the Respondents, Gwin, also residents of Alabama. Their sales agreement required Gwin to transfer "[t]he current termite contract, if any" to Dobson.[1] The house was inspected by local employees of

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[1] The sales agreement also required Gwin to furnish written evidence from a termite control company that a visual inspection of the residence indicated that the dwelling was free from infestation by wood destroying insects and damage caused by a currently active infestation. Terminix furnished such evidence to Dobson, at closing. That evidence, and the inspection on which it was based, is the subject of claims by Dobson against Terminix for negligence, wanton misconduct and misrepresentation. (R. 1-5) Dobson contends that those tort claims arose prior to the time that there was any contractual relationship with Terminix and that those claims are, therefore, not within the scope of the arbitration clause. That issue was not reached by the court below.

Also, Dobson contends that because they did not sign the termite protection plan, but that it was transferred to them by the unilateral act of Terminix, at the request of Gwin, they are

Terminix Service (R. 1613-28) and Gwin's termite protection plan was transferred to Dobson by a typewritten notation on the face of the Gwin contract. (R. 1673) Before the Alabama Supreme Court, Petitioners pointed to four facts which, it was contended, evidence a transaction involving commerce. (A. 6a-7a)[2] First, Petitioners rely on the fact that Terminix Service is an Arkansas corporation and Terminix International is a limited partnership with its principal place of business in Memphis, Tennessee. Next, Petitioners argue that most of the materials and equipment, including specifically the chemicals used to treat the home involved here, were purchased by Terminix Service outside Alabama. (R. 272-73) Also, Petitioners argue that the termite protection plan contained language recognizing that Terminix performs its services in accordance with the requirements of federal, state and local law. (R. 279, para. 6) And, finally, it is contended that the Dobson contract involves commerce because Gwin, when they first bought the Terminix plan in 1987, did so out of a desire to "go with a national company like Terminix." (R. 1346)

We are aware of no decision holding that the mere fact that parties to a contract are residents of different states is, of itself, proof that their transaction involves commerce. *See Maxum Foundation, Inc. v. Salus Corporation*, 779 F.2d 974, 978 n.4 (4th Cir. 1985).

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not bound by the arbitration clause contained in the plan. That issue was also not reached by the court below.

[2] Citations to "A" are to the Appendix attached to the Petition for a Writ of Certiorari.

To the extent that chemicals may have been bought elsewhere and brought into Alabama for use in treating the Dobson home, that kind of activity is merely incidental to the transaction which is "evidenced by" the contract. Stated otherwise, there is nothing in the Terminix contract "evidencing" a contract to bring chemicals into Alabama. The transaction, as is plainly set forth in the plan, is for "the necessary service to protect the identified property against the attack of subterranean termites . . ." (R. 287) The heart of the transaction is the service provided, a purely local function, including the skill, expertise and knowledge necessary to see that the house is protected from termites. Obviously, that could, but would not necessarily, include the use of chemicals which might or might not be bought outside Alabama, just as the gasoline in the tank of the serviceman's truck might or might not be refined outside Alabama. There is nothing in the decisions of this Court or in the language or history of the Act, however, which indicate a Congressional intent to define the term "involving commerce" to such an extent. This same argument applies concerning the provision in the contract recognizing that the service provided by Terminix is performed in accordance with federal, as well as state and local laws.

Finally, the fact that Gwin may have been motivated by an uncommunicated desire to "go with a national company like Terminix" is not evidence that the transaction itself involves commerce. Also, Gwin's motivation can hardly be evidence of the nature of the transaction between Dobson and Terminix.

It is difficult to imagine a more local transaction than purchasing a home. The same is true of agreements to

service the home, including those to insure that it is free from termites. Now it is contended that this transaction involves interstate commerce. Without question, the parties to this transaction did not contemplate their involvement in interstate commerce. But, further, we submit that neither did their transaction have a "slight nexus" with commerce, regardless of what they contemplated.

II. THE CASES CITED BY PETITIONERS DO NOT SUPPORT THE CONTENTION THAT THERE IS A DIVISION OF AUTHORITY AMONG STATE AND FEDERAL COURTS CONSTRUING SECTION 2.

In support of its position that there exists a division of authority, Petitioners cite five cases illustrating the point that, on the one hand, most courts addressing the issue have held that the phrase "contract evidencing a transaction involving commerce" must be broadly construed.[3] An examination of the facts involved in those cases, however, leads to the conclusion that the underlying transaction in each case would likely be found to involve commerce, no matter what standard was applied. For instance, *Snyder v. Smith, supra,* after suggesting that

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[3] *Snyder v. Smith,* 736 F.2d 409 (7th Cir. 1984); *Societe Generale de Surveillance, S.A. v. Raytheon European Management and Systems Company,* 643 F.2d 863 (1st Cir. 1981); *Foster v. Turley,* 808 F.2d 38 (10th Cir. 1986); *Del E. Webb Construction v. Richardson Hospital Authority,* 823 F.2d 145 (1st Cir. 1987); *Woermann Construction Co. v. Southwestern Bell Tel. Co.,* 846 S.W.2d 790 (Mo.Ct.App., 1993). It should be noted that the *Woermann* decision is not from a "state court of last resort" within the meaning of Rule 10.1 of the Rules of the Supreme Court of the United States.

the "involving commerce" language of the Act was as broad as Congress' power to regulate under the commerce clause, held that

> [w]e need not decide today whether Congress intended the FAA to apply to all contracts affecting interstate commerce, for it is clear that the partnership agreement presented in this case falls well within the constitutional limits. The real estate at issue was located in Texas; the partners lived in, and the partnership was managed from, Illinois. The partnership borrowed money from and maintained a checking account with a bank in Illinois. Thus, the partnership agreement involved interstate commerce and the FAA is applicable. *Id.* at 418.

Foster v. Turley, supra, referred to the dicta in *Snyder* concerning the breadth of the "involving commerce" language before concluding that the Act applied to a partnership agreement to sell ore from a New Mexico mine "all over the country." 808 F.2d 38, at 40. And *Societe Generale de Surveillance, S.A., supra,* found the Act to apply to a contract between French and American companies concerning the transportation and testing in Europe of missiles made in California and Massachusetts. 643 F.2d 863, at 867. Therefore, these cases and the others cited in this line by Petitioners[4] are decided on facts

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[4] *Del E. Webb, supra,* another of the cases cited in this line by Petitioner, recognized that the term "involving commerce" had been held to mean more than transactions for the interstate shipment of goods and that it included contracts "relating to interstate commerce." 823 F.2d 145, at 147-48. But that case involved a contract to build an expansion and renovation of a medical center in Texas, requiring employees of the contractor

which clearly involve commerce, regardless of the test employed.

The opposing line of cases cited by Petitioners[5] does not take the narrow view of the meaning of the phrase "a transaction involving commerce" as is contended by Petitioners. Rather, the cases in that line adopt quite the opposite view. That is, while those cases do cite the concurring opinion of Judge Lumbard in *Metro Industrial Painting Corp. v. Terminal Construction Company, Inc.*, 237 F.2d 382 (2d Cir. 1961) (hereinafter referred to as "*Metro Industrial*"), they do so in an effort to *broaden* the construction of the term "involving commerce" not narrow it. For instance, in *Burke County, supra*, the issue involved the design of a school in North Carolina by a multi-state architectural firm. The North Carolina Court of Appeals had ruled that the Act did not apply because it did not

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to travel interstate and materials for the facility to be manufactured and moved interstate. *Woermann, supra*, relied on *Del E. Webb* to reach the conclusion that "construction contracts performed in one state which require materials from another state, fall under the umbrella of the FAA." 846 S.W.2d 790, at 793. *Woermann* then found the Act to apply to a construction contract for Southwestern Bell, in Missouri, where the mechanical equipment used in the project came from out of state.

[5] *Burke Co. Public Schools Bd. of Educ. v. Shaver Partnership*, 279 S.E.2d 816 (N.C. 1981); *Pathman Const. Co. v. Knox County Hospital Ass'n.*, 326 N.E.2d 844 (Ind.Ct.App. 1975); *R. J. Palmer Const. Co., Inc. v. Wichita Band Instrument Co., Inc.*, 642 P.2d 127 (Kan.Ct.App. 1982); *Loche v. Dean Witter Reynolds, Inc.*, 526 N.E.2d 1296 (Mass.App.Ct. 1988); *Lacheney v. Profitkey Int'l, Inc.*, 818 F.Supp. 922 (E.D.Va. 1993). We would note that of these decisions only *Burke County* is from a "state court of last resort" within the context of Rule 10.1 of the Rules of the Supreme Court of the United States.

involve or relate to the "actual physical interstate shipment of goods." *Id.* at 818-819. In reversing, the North Carolina Supreme Court held that the

> [r]eliance by Plaintiff and our Court of Appeals on *San Carlo Opera Co.*, [163 F.2d 310 (2d Cir. 1947)], is misplaced as the Second Circuit would in fact reject, as we do, the narrow view of the federal act's applicability fashioned by our Court of Appeals. *Id.* at 821.

The North Carolina Supreme Court went on to state its test, based on the concurring opinion in *Metro Industrial*, as follows:

> Where, however, performance of the contract itself necessarily involves, so that the parties to the agreement must have contemplated, substantial interstate activity, the contract evidences a transaction involving commerce within the meaning of the Federal Arbitration Act. *Id.* at 822 (footnote omitted).

R. J. Palmer Construction Company, supra, also illustrates the point that the courts in this line of cases see the "contemplation" standard as broader than the "slight nexus" or "involving-in-fact" standard. That case involved the construction of a building in Kansas using redwood siding, which, the Court found, the parties had contemplated being brought from out of state. The Court there went on to hold that

> [i]n addition, the building presumably was to be used to house and sell musical instruments and related items that would be moved in interstate commerce, a fact which would have been known to all parties when the agreement was entered into. *Id.* at 130.

That is, the Court, in effect, reasoned that even though there had apparently been no sale of goods, in fact, from the building, the parties had contemplated such sales and the transaction, therefore, would, in the future, involve commerce. In that situation, the contemplation standard is obviously broader, involving a more liberal application of the Act.

To the extent that any of the cases cited in this line by Petitioners depend for their result on the test employed, it seems clear that they relied on the contemplation standard to broaden, not narrow, the inquiry.[6] Significantly, each of the five cases cited by Petitioners as representing the "opposing view" found the Act to apply because the transaction at issue involved commerce. That does not indicate a line of authority holding to a "narrow view" of the statute. We submit that those cases do not represent a part of a trend to disregard a liberal federal policy favoring arbitration, but, to the contrary, are consistent with

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[6] *Lacheney v. Profitkey International, Inc., supra,* involves the same reasoning. There, the transaction involved a franchising agreement to sell computer software, although apparently none had, in fact, been sold. Nevertheless, the Court held, the parties contemplated such a sale and the Act applied. *Loche v. Dean Witter Reynolds, supra,* noted that the contract at issue there "contemplated a continuing investment relationship, much of it *necessarily* involving interstate commerce." *Id.* at 1300 (emphasis added). *Pathman Construction Company, supra,* expressly cited the concurring opinion in *Metro Industrial* for the proposition that "[i]n addition to *Prima* [*Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, 388 U.S. 395 (1967)], numerous other courts have considered the question here presented and have generally held that the Act, in this respect, should receive a liberal construction." *Id.* at 852.

the *Snyder v. Smith* line of cases in their result and, for the most part, in their rationale. That they employ the contemplation of the parties rationale to reach that result does not constitute a "special and important reason" for this Court to grant the Writ to resolve a division of authority or lack of uniformity on this federal question.

III. THE "CONTEMPLATION OF THE PARTIES" TEST DOES NOT CONFLICT WITH ANY DECISION OF THE SUPREME COURT CONSTRUING SECTION 2.

It is undisputed that this Court has interpreted Section 2 as a congressional declaration of a liberal federal policy favoring arbitration agreements. That interpretation has been recognized and applied by the Alabama Supreme Court. *See, e.g., Shearson Lehman Brothers, Inc. v. Crisp,* Case No. 1910090, 1992 Lexis 909 (August 14, 1992). In fact, on the same day the Alabama Supreme Court announced its adoption of the contemplation of the parties test in *Ex Parte Jones,* Case No. 1920249, 1993 Ala. Lexis 662 (July 16, 1993), it also released its opinion in *Continental Grain Company, Inc. v. Beasley,* Case No. 1920241, 1993 Ala. Lexis 669 (July 16, 1993). In *Continental Grain,* the Alabama Supreme Court held the Federal Arbitration Act to apply, based on the contemplation of the parties test, where chicken growers residing in Alabama sold their product in other states and countries. Although the growers argued that their contracts were performed entirely within Alabama, the court there held that they had contemplated substantial interstate activity.

This Court has not defined the precise limits of the field of operation of the Act. It has, however, rendered two decisions touching on that issue. In *Bernhardt v. Polygraphic Company of America, Inc.*, 350 U.S. 198 (1956), this Court had before it an employment contract between a New York corporation and a resident of New York who was being employed as a plant superintendent to work at a Vermont plant site operated by the company.[7] One of the issues before this Court was whether that contract evidenced a transaction involving commerce. This Court held that it did not because

> [t]here is no showing that petitioner, while performing his duties under the employment contract was working "in" commerce, was producing goods for commerce, or was engaging in activity that affected commerce, within the meaning of our decisions. *Id.* at 201 (footnote omitted).

Whatever other conclusions might be drawn from the decision in *Bernhardt*, it is clear that this Court construed the Act to mean that not all contracts are covered by the Act. That holding was also in the context of an employee being sent across state lines to work at a business or industrial site. Similarly, in *Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, 388 U.S. 395 (1967), this Court was presented with the question whether interstate commerce

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[7] These facts are largely gleaned from the opinion of the Court of Appeals in the same case, which was before the Supreme Court on certiorari. See *Bernhardt v. Polygraphic Co. of America*, 218 F.2d 948 (2d Cir. 1955).

was involved where the underlying transaction concerned a consulting agreement with a paint business having 175 wholesale clients in a number of states. The agreement secured the assistance of one of the parties "in arranging the transfer of manufacturing and selling operations from New Jersey to Maryland." *Id.* at 401 (footnote omitted). That transaction, this Court held, involved commerce. In so holding, the majority opinion rejected a dissenting opinion to the effect that the term "involving commerce" should be construed to apply only to "contracts between merchants for the interstate shipment of goods." *Id.* at 401, n.7.

Therefore, without prescribing any particular test or standard for other courts to follow in resolving this issue, this Court has ruled on two specific examples of transactions, one of which involves commerce and one of which does not. That some courts have chosen to structure their analysis of cases raising this issue in terms of what the parties contemplated their transaction to include does not appear to be inconsistent with the holding in either of these cases.[8] We would suggest that it is more important to examine the result obtained, based on any particular set of facts, rather than the method of reaching that result. As we demonstrated above, the result obtained in the cases relied on by Petitioners are remarkably uniform.

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[8] In fact, the concurring opinion of Judge Lumbard in *Metro Industrial*, which is the object of Petitioners' criticism in this case, was cited with approval by this Court in its opinion in *Southland Corp. v. Keating*, 465 U.S. 1 (1984), wherein this Court quoted that concurring opinion concerning the purpose of the Act. *Southland*, 465 U.S. 1 at 13-14.

Petitioners rely heavily on *Perry v. Thomas*, 482 U.S. 483 (1987). That case does not, we would submit, hold that the Act evidences a congressional intent to enforce arbitration agreements "within the full reach of the Commerce Clause." We read *Perry* to hold that as to contracts which *are* covered by the Act, they are *exclusively* covered by the Act and that contrary state laws are preempted and, therefore, invalid. *Perry*, we would suggest, does not speak to the question of which contracts are covered by the Act, which is the issue here.

CONCLUSION

The Petition for a Writ of Certiorari should be denied.

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Nos. 93-1000 and 93-1001

IN THE

Supreme Court of the United States

OCTOBER TERM, 1993

THE TERMINIX INTERNATIONAL COMPANY LIMITED PARTNERSHIP and ALLIED-BRUCE TERMINIX COMPANIES, INC.,

Petitioners,

v.

MARK JACKSON and LAURIE JACKSON,

Respondents.

ALLIED-BRUCE TERMINIX COMPANIES, INC., and TERMINIX INTERNATIONAL COMPANY,

Petitioners,

v.

G. MICHAEL DOBSON, WANDA C. DOBSON, STEVEN GWIN and JAN GWIN,

Respondents.

On Petition for Writs of Certiorari to the Supreme Court of Alabama

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REPLY BRIEF FOR PETITIONERS

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REPLY BRIEF FOR PETITIONERS

The petitions in these cases made two principal points: that different courts have employed markedly different approaches in deciding whether Section 2 of the Federal Arbitration Act makes agreements to arbitrate enforceable as a matter of federal law; and that the court below—in aligning itself with courts that apply Section 2 only when the parties "contemplated substantial inter-

state activity" at the time of their agreement—had chosen a reading of Section 2 that is contrary to both its language and purpose. In their briefs in response, respondents do not seriously argue that Congress intended to make agreements to arbitrate enforceable only if the parties "contemplated substantial interstate activity": indeed, neither brief makes any effort to defend that standard by reference to the language of Section 2, or its underlying policies, at all. Rather, the briefs simply contend, in a number of related ways, that the conflict among state and federal courts on this issue should be treated as immaterial. These contentions are uniformly unpersuasive.

1. The Dobson respondents initially argue that the transaction at issue here would not fall within the terms of Section 2 under *any* test currently being applied by state and federal courts. Dobson Br. at 3-6. But respondents' own discussion proves just the opposite. Although the facts set out in their brief—showing an agreement among parties in different states and the use of materials shipped in interstate commerce—were held insufficient by the Alabama Supreme Court to demonstrate that the parties "contemplated substantial interstate activity" (Pet. App. 6a-7a), they plainly *do* demonstrate a sufficient nexus to interstate commerce under the test employed by most federal courts. The Tenth Circuit has held, for example, that "[t]he requirement that the underlying transaction involve commerce is to be broadly construed so as to be coextensive with congressional power to regulate under the Commerce Clause," *Foster v. Turley*, 808 F.2d 38, 40 (10th Cir. 1986), and it is beyond question that Congress would have the "power . . . under the Commerce Clause" to regulate transactions between parties in different states involving materials that move in interstate commerce. Thus, in this case as in many others, the choice regarding the test to be applied is dispositive with regard to whether an agreement to

arbitrate is or is not enforceable as a matter of federal law.[1]

2. The principal thrust of respondent Dobsons' brief, echoed in respondent Jacksons' brief, is that the Court need not be concerned about the different tests for applying Section 2 that are employed by different courts. Dobson Br. at 6-11; Jackson Br. at 6-9. In particular, the Dobson respondents argue that the courts adopting the contemplation-of-the-parties test "do so in an effort to *broaden* the construction of the term 'involving commerce' not narrow it." Dobson Br. at 8. This argument is faulty on a number of grounds.

To begin with, it is nonsensical to say that a test requiring contemplation of *substantial* interstate activity will subject more transactions to the reach of federal law than a test requiring only a slight nexus with interstate activity.[2] Indeed, the former test—articulated by Judge Lumbard in *Metro Indus. Painting Corp. v. Terminal Constr. Co.*, 287 F.2d 382 (2d Cir.), *cert. denied*, 368 U.S. 817 (1961) (concurring opinion)—grew out of Judge Lumbard's disagreement with the view, taken by

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[1] The Dobson respondents do not dispute that the transaction *in fact* involved materials shipped in interstate commerce; rather, they say that this interstate movement would not "necessarily" occur in every case. Dobson Br. at 5. But that is simply another way of saying that the parties would not necessarily "contemplate" that activity at the time of their agreement. Under the standard adopted by the court below, of course, the fact of interstate commerce is not enough to require application of Section 2. It *is* enough under the test applied by most other courts.

[2] It is possible that the parties might contemplate substantial interstate activity in a transaction that, for some reason, turns out not to involve any at all. But it seems highly doubtful that courts employing the contemplation-of-the-parties test would actually find Section 2 applicable in those circumstances and, if they did so, it would raise serious questions about the power of Congress to preempt state law with respect to transactions having no nexus in fact to interstate commerce.

the Second Circuit in a previous case, that "Congress intended to use to the fullest possible extent its powers to regulate commerce as it was affected by arbitration agreements." *See id.* at 386 (quoting *Robert Lawrence Co. v. Devonshire Fabrics, Inc.*, 271 F.2d 402, 407 (2d Cir. 1959), *cert. granted*, 362 U.S. 909 (1960), *cert. dismissed pursuant to stipulation*, 364 U.S. 801 (1960)). Judge Lumbard was instead of the opinion that the federal courts "must be cautious in construing the act lest we excessively encroach on the powers which Congressional policy, if not the Constitution, would reserve to the states." 287 F.2d at 386. Given that approach, it is hardly surprising that the test not only requires that the parties actually contemplate interstate activity but that the interstate activity, in addition, be substantial.

It is also crystal clear that—even if some other court thought so—the *Alabama Supreme* Court does *not* think that the test is "broader" than the actual nexus test. Indeed, that court has flatly stated that it elected to apply the contemplation-of-the-parties test because it "better promotes our strong public policy *against* the use of predispute arbitration agreements." *Lopez v. Home Buyers Warranty Corp.*, 628 So. 2d 361, 363 n.2 (Ala. 1993), *petition for cert. filed*, 62 U.S.L.W. 3430 (Dec. 22, 1993) (No. 93-995) (emphasis added).[3] This declaration, not mentioned by respondents, shows two things: first, that the test does restrict the application of Section 2 and, second, that it may be deliberately employed for that purpose by courts hostile to federal policy.

In any event, the relevant issue ultimately is not whether one test is broader or narrower than the other, but whether the test used below properly reflects Congress' intent in

[3] Since the petitions in these cases were filed, the Alabama Supreme Court has reaffirmed its commitment to the contemplation-of-the-parties test, again using it to deny enforcement of an agreement to arbitrate. *Ex Parte Lorance*, No. 1930140, 1994 Ala. LEXIS 62 (Sup. Ct. Feb. 11, 1994).

enacting Section 2. This Court has said that "the Federal Arbitration Act . . . embodies Congress' intent to provide for the enforcement of arbitration agreements within the full reach of the Commerce Clause." *Perry v. Thomas*, 482 U.S. 483, 490 (1987). As we have set out in the petitions, *see, e.g.*, Dobson Pet. at 8-12, the contemplation-of-the-parties test finds no basis in either the language of Section 2 (which speaks objectively of "transaction[s] involving commerce") or in its purpose (to put arbitration contracts on the same footing as all other contracts). It thus imposes an unjustified limitation on the power of Congress to make arbitration agreements fully enforceable as a matter of federal law.

3. This Court has expressed an "unwilling[ness] to attribute to Congress the intent, in drawing on the comprehensive powers of the Commerce Clause, to create a right to enforce an arbitration contract and yet make the right dependent for its enforcement on the particular forum in which it is asserted." *Southland Corp. v. Keating*, 465 U.S. 1, 15 (1984) (holding that Section 2 must be applied in state as well as federal courts). But, if state and federal courts are free to interpret Section 2 in light of their own preferences about the enforceability of arbitration agreements, the scope of federal law will necessarily depend "on the particular forum in which it is asserted." *Id.* Thus, whatever the correct standard may be, a lack of uniformity in the application of Section 2 is flatly inconsistent with Congress' efforts to "create a body of federal substantive law of arbitrability, applicable to *any* arbitration agreement within the coverage of the Act." *Moses H. Cone Memorial Hosp. v. Mercury Constr. Corp.*, 460 U.S. 1, 24 (1983) (emphasis added). This Court should grant review to correct it.

CONCLUSION

The petitions for writs of certiorari should be granted.

Respectfully submitted,

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In The

Supreme Court of the United States

October Term, 1993

ALLIED-BRUCE TERMINIX COMPANIES, INC., ET AL.,

Petitioners,

v.

G. MICHAEL DOBSON, ET AL.,

Respondents.

Petition For A Writ Of Certiorari To The Supreme Court Of Alabama

MOTION OF THE ALABAMA WATER AND SEWER INSTITUTE AND THE ALABAMA MANUFACTURED HOUSING INSTITUTE FOR LEAVE TO FILE BRIEF AS *AMICI CURIAE* IN SUPPORT OF THE PETITION FOR A WRIT OF CERTIORARI

AND

BRIEF OF THE ALABAMA WATER AND SEWER INSTITUTE AND THE ALABAMA MANUFACTURED HOUSING INSTITUTE AS *AMICI CURIAE* IN SUPPORT OF THE PETITION FOR A WRIT OF CERTIORARI

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The Alabama Water and Sewer Institute and the Alabama Manufactured Housing Institute respectfully move this Court for leave to file the accompanying brief in this case as *amici curiae*. The consent of counsel for the petitioners herein has been obtained, but counsel for the respondents herein have refused to consent to the filing of a brief by the Alabama Water and Sewer Institute and the Alabama Manufactured Housing Institute as *amici curiae*.

The Alabama Water and Sewer Institute (hereinafter "AWSI") is a non-profit organization representing thirteen of the largest water producers in the State of Alabama. Its members are public corporations and municipal boards organized and existing pursuant to Acts of the Legislature of Alabama for the purpose of operating water and/or sanitary sewer facilities within the State of Alabama.

The applicant, AWSI, has an interest in this case in that the members of AWSI regularly enter into contracts in the State of Alabama containing arbitration clauses substantially similar to that at issue in the instant case. Said contracts include agreements for engineering services and other professional services, for construction of public facilities, and for the purchase or lease of real and personal property. The members of AWSI have an interest in state court enforcement of agreements to submit disputes arising from these contracts to binding arbitration in order to control the increasing costs of litigation that drain funds designated for public purposes. The refusal of the courts of the State of Alabama to enforce such arbitration clauses substantially impairs the rights of the members of AWSI under said contracts.

The Alabama Manufactured Housing Institute (hereinafter "AMHI") is a non-profit trade association representing all segments of the manufactured housing industry. Its members include nearly 450 manufactured home manufacturers, retailers, parts suppliers, providers of services including delivery and installation, finance and insurance companies, park owners and developers.

The applicant, AMHI, has an interest in this case in that the members of AMHI regularly enter into contracts in the State of Alabama containing arbitration clauses substantially similar to that at issue in the instant case. The members of AMHI have an interest in state court enforcement of agreements to submit disputes arising from these contracts to binding arbitration in order to control the increasing costs of litigation affecting all aspects of the manufactured home industry. The refusal of the courts of the State of Alabama to enforce such arbitration clauses substantially impairs the rights of the members of AMHI under said contracts.

The brief of the petitioners herein in the Supreme Court of Alabama argues that the Federal Arbitration Act applies to any agreement having the slightest nexus with interstate commerce. However, the discussion therein does not address the manner in which the intent of Congress in passing the Federal Arbitration Act, to supersede all state restrictions on the enforceability of arbitration clauses to the fullest extent possible under the Commerce Clause of the United States Constitution, has been thwarted by inconsistent applications of the Federal Arbitration Act by state courts and federal circuit courts of appeals throughout the country, most particularly in the inconsistent tests applied by the Eleventh Circuit Court of Appeals and the Alabama Supreme Court. AWSI and AMHI have no reason to believe that the argument on this point will be expanded and be made complete in this Court.

If applicants' argument is approved by this Court, the decision of the court below must be reversed.

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BRIEF OF THE ALABAMA WATER AND SEWER INSTITUTE AND THE ALABAMA MANUFACTURED HOUSING INSTITUTE AS *AMICI CURIAE* IN SUPPORT OF THE PETITION FOR A WRIT OF CERTIORARI

QUESTION PRESENTED

Section 2 of the Federal Arbitration Act, 9 U.S.C. § 2, makes an agreement to arbitrate enforceable, as a matter of federal law, provided that it is part of "a contract evidencing a transaction involving commerce." The question presented here is as follows:

Whether the Alabama Supreme Court correctly held – contrary to the view taken by most state and federal courts – that Section 2 is inapplicable to contracts otherwise involving interstate commerce if the parties did not "contemplate[] substantial interstate activity" at the time of the contract.

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No. 93-1001

In The

Supreme Court of the United States

October Term, 1993

ALLIED-BRUCE TERMINIX COMPANIES, INC., ET AL.,

Petitioners,

v.

G. MICHAEL DOBSON, ET AL.,

Respondents.

Petition For A Writ Of Certiorari To The Supreme Court Of Alabama

THE ALABAMA WATER AND SEWER INSTITUTE AND THE ALABAMA MANUFACTURED HOUSING INSTITUTE RESPECTFULLY SUBMIT THE FOLLOWING BRIEF IN SUPPORT OF PETITIONERS AS *AMICI CURIAE*.

INTEREST OF AMICI CURIAE

The Alabama Water and Sewer Institute (hereinafter "AWSI") is a non-profit organization representing thirteen of the largest water producers in the State of Alabama. Its members are public corporations and municipal boards organized and existing pursuant to Acts of the Legislature of Alabama for the purpose of operating water and/or sanitary sewer facilities within the State of Alabama.

The Applicant has an interest in this case in that the members of AWSI regularly enter into contracts in the State of Alabama containing arbitration clauses substantially similar to that at issue in the instant case. Said contracts include agreements for engineering services and other professional services, for construction of public facilities, and for the purchase and lease of real and personal property. The members of AWSI have an interest in state court enforcement of agreements to submit disputes arising from these contracts to binding arbitration in order to control the increasing costs of litigation that drain funds designated for public purposes. The refusal of the courts of the State of Alabama to enforce such arbitration clauses substantially impairs the rights of the members of AWSI under said contracts.

The Alabama Manufactured Housing Institute (hereinafter "AMHI") is a non-profit trade association representing all segments of the manufactured housing industry. Its members include nearly 450 manufactured home manufacturers, retailers, parts suppliers, providers of services including delivery and installation, finance and insurance companies, park owners and developers.

The applicant, AMHI, has an interest in this case in that the members of AMHI regularly enter into contracts in the State of Alabama containing arbitration clauses substantially similar to that at issue in the instant case. The members of AMHI have an interest in state court enforcement of agreements to submit disputes arising from these contracts to binding arbitration in order to control the increasing costs of litigation affecting all aspects of the manufactured home industry. The refusal of the courts of the State of Alabama to enforce such

arbitration clauses substantially impairs the rights of the members of AMHI under said contracts.

Petitions for Writs of Certiorari to the Alabama Supreme Court involving the same issue presented in the instant case are pending before this Court in *Terminix International Company Limited Partnership and Allied-Bruce Terminix Companies, Inc., v. Jackson*, [1911842], ___ So. 2d ___ (Ala. 1993), and in *Lopez v. Home Buyers Warranty Corporation*, [1920330], ___ So. 2d ___ (Ala. 1993). Applicants' arguments herein also support the positions advocated by the said petitioners in these related cases.

ARGUMENT

It is well established that Congress has the power under the United States Constitution to regulate activities "affecting" interstate commerce. *Habersham Mills v. F.E.R.C.*, 976 F.2d 1381, 1384 (11th Cir. 1992). The Federal Arbitration Act (hereinafter "FAA") provides that arbitration clauses in contracts "involving commerce," where commerce is defined as "commerce among the several States," shall be enforceable. 9 U.S.C. § 2. The issue in the present case arises because many federal circuit courts of appeals and state courts interpret the phrase "contracts involving commerce among the several States," as used in the FAA, to invoke less power than Congress has under the Commerce Clause to regulate activities "affecting" interstate commerce. In short, many federal courts and state courts have disregarded the precedent of this Court requiring that the FAA be applied to the full extent of Congressional power under the Commerce Clause. As a

result there is a serious and growing conflict as to the scope of the FAA. If the FAA is not given a uniform interpretation, parties to arbitration agreements will be subject to different outcomes depending upon the jurisdiction in which the action to compel arbitration is brought. The limitation on the applicability of the FAA is plainly contrary to the opinions of this Court. This Court stated in *Perry v. Thomas*, 482 U.S. 483, 490 (1987), that the FAA provides "for the enforcement of arbitration agreements within the full reach of the Commerce Clause." It is clear that the FAA is based upon the commerce power of Congress, and that contracts are to be construed liberally in favor of arbitration. *Southland Corp. v. Keating*, 465 U.S. 1, 12-13 (1984) ("[T]he [FAA] was an exercise of the Commerce Clause power."); *Moses H. Cone Memorial Hospital v. Mercury Construction Co.*, 460 U.S. 1, 24 (1983) ("Section 2 [of the FAA] is a congressional declaration of a liberal federal policy favoring arbitration agreements, notwithstanding any state substantive or procedural policies to the contrary."); *Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, 388 U.S. 395, 401 (1967)("It is clear beyond dispute that the federal arbitration statute is based upon and confined to the incontestable federal foundations of 'control over interstate commerce and over admiralty.'"); *See also Bernhardt v. Polygraphic Company*, 350 U.S. 198, 200-201 (1956). Moreover, this Court has unequivocally stated that "[t]he purpose of the [FAA] was to assure those who desired arbitration and whose contracts related to interstate commerce that their expectations would not be undermined by . . . state courts." *Southland Corp. v. Keating*, 465 U.S. 1, 13 (1984).

At the present time a majority of federal circuit courts of appeals and a minority of state courts correctly interpret the term "involving commerce" to bring within the FAA all contracts that Congress could constitutionally regulate under the Commerce Clause.[1] However, a minority of the federal circuit courts of appeals and a majority

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[1] *E.g., Del E. Webb Const. v. Richardson*, 823 F.2d 145,147 (5th Cir. 1987) (A contract comes under the FAA so long as it simply relates to interstate commerce.); *Mesa Operating Ltd. Partnership v. Louisiana Intrastate Gas Corp.*, 797 F.2d 238, 243 (5th Cir. 1986) ("Commerce" under the FAA includes all contracts relating to interstate commerce.); *American Airlines, Inc. v. Louisville and Jefferson County Air Board*, 269 F.2d 811 (6th Cir. 1959) (FAA was enacted in exercise of Congress' plenary power over interstate commerce.); *Snyder v. Smith*, 736 F.2d 409 (7th. Cir. 1984) (The breadth of "involving commerce" is equated with the extent of Congress's power to regulate under the commerce clause; Congress intended the FAA to extend to all contracts that it could constitutionally regulate.); *First Investors Corp. v. American Capital Financial Services, Inc.*, 823 F.2d 307 (9th Cir. 1987) (FAA governs agreements "affecting" interstate commerce.); *Foster v. Turley*, 808 F.2d 38 (10th Cir. 1986) (Requirement of FAA that underlying transaction involve commerce is to be broadly construed so as to be coextensive with congressional power to regulate under the Commerce Clause.); *Shatel Corp. v. Mao Ta Lumber and Yacht Corp.*, 697 F.2d 1352, 1354 (11th Cir. 1983) ("Commerce" includes any intrastate transaction which "affects" interstate commerce.); *G.D. Searle & Co. v. Metric Constructors, Inc.*, 572 F.Supp. 836 (N.D.Ga. 1983) (It has consistently been noted that federal policy favors arbitration and that the statute should be broadly applied.); *Fairchild & Co., Inc. v. Richmond, F. & P.R. Co.*, 516 F.Supp. 1305 (D.C.D.C. 1981) ("[I]nvolving commerce" as used in FAA is not to be narrowly construed as "commerce" reaches not only the actual physical interstate shipment of goods but also contracts relating to interstate commerce.); *John W. Johnson, Inc. v. 2500 Wisconsin Ave.*, 231 F.2d 761 (D.C.Cir. 1956); *Henry v. Alcove Inv., Inc.*, 284 Cal.Rptr. 255 (Cal.App. 2 Dist. 1991) (A transaction must have an effect on

of state courts still have not explicitly stated whether the FAA applies to all contracts within the power of Congress. Many of these courts continue to restrict the application of the FAA, giving the FAA less force than the Commerce Clause provides. These courts appear merely to count the contacts between the parties and relevant states to determine whether the FAA applies. As a result, the outcome of actions to enforce arbitration in these jurisdictions is inevitably arbitrary and uncertain.[2]

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interstate commerce.); *Van Luven v. Rooney, Pace Inc.*, 241 Cal.Rptr. 248 (Cal.App. 4 Dist. 1987) (finding a liberal federal policy favoring arbitration); *Weber v. White Eagle Golf Club*, 608 N.E.2d 595 (Ill.App.3 Dist. 1993) (holding that any doubts should be resolved in favor of arbitration); *Flower World of America, Inc. v. Whittington*, 385 A.2d 85, 89 (Md. 1978) (The FAA is based upon and confined to the uncontestable federal foundations of control over interstate commerce.); *Woermann Const. v. Southwestern Bell*, 846 S.W.2d 790, 792 (Mo.App.E.D. 1993) (A contract comes under the Federal Arbitration Act so long as it simply relates to interstate commerce.).

[2] *E.g., Dickstein v. DuPont*, 443 F.2d 783 (1st Cir. 1971) (Contract was not a transaction involving commerce since there was no movement of goods across state lines.); *Thomas O'Connor & Co., Inc. v. Insurance Co. of North America*, 697 F.Supp. 563 (D.Mass. 1988) (Construction contract involved commerce where New York contractor performed work in New Jersey, materials came from outside New Jersey, and subcontractor was citizen of Massachusetts.); *New Castle County v. U.S. Fire Ins. Co.*, 728 F.Supp. 318 (D.Del. 1989) (Settlement agreement between insurer and county, who were citizens of different states, which involved at least $184,000 was a contract involving commerce under the FAA.); *Goodwin v. Elkins & Co.*, 730 F.2d 99, *cert. denied* 105 S.Ct. 118 (3rd Cir. 1984); *compare Kirschner v. West Co.*, 185 F.Supp. 317, 319 (D.C.Pa. 1960) ("Commerce" means the type of commerce which is within federal jurisdiction, that is, interstate or foreign commerce.); *AM. Home Assur. v. Vecco Concrete Const.*,

Moreover, a growing minority of state courts have explicitly adopted a very restrictive standard for

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Etc., 629 F.2d 961 (4th Cir. 1980) (Transaction between Delaware Corporation, with its principal place of business in Alabama, and Virginia Corporation, which included subcontracts and purchase orders for products and equipment shipped to Virginia from Maryland, Alabama, Utah, Missouri and California, which employed non-residents in the project, and used a New York bonding company to guarantee performance, clearly demonstrated that the contract was one evidencing a transaction involving interstate commerce as contemplated by the FAA.); *Mutual Reinsurance Bureau v. Great Plains Mut. Ins. Co., Inc.*, 750 F.Supp. 455 (D.C.Kan. 1990) (Reinsurance agreement between two insurers involved interstate commerce within the FAA even though contract negotiations transpired within Kansas, where parties were of diverse citizenship, the agreement was originally drafted in Illinois, and business was transacted over the telephone and through the mail.); *Axtell v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 744 F.Supp. 194, 195 (E.D.Ark. 1989) (Customer agreement signed by investors that contained arbitration agreement affected "commerce" within the meaning of the FAA.); *compare Seymour v. Gloria Jean's Coffee Bean Franchising Corp.*, 732 F.Supp. 988 (D.Minn. 1990) (Federal Arbitration Act is based on congressional power to regulate interstate commerce.); *England v. Dean Witter Reynolds, Inc.*, 811 S.W.2d 313 (Ark. 1991) (Employment contract to work for securities broker was contract involving interstate commerce.); *McEntire v. Monarch Feed Mills*, 631 S.W.2d 307 (Ark. 1982) (Contract involved interstate commerce where Missouri based grain purchaser with manufacturing facilities in Missouri and Arkansas contracted to purchase grain from farmer in Arkansas for delivery to its manufacturing plant in Arkansas.); *Ayers v. Prudential-Bache Securities*, 762 P.2d 743 (Colo.App. 1988) (citing *Robinson v. Bache & Co.*, 227 F.Supp. 456 (S.D.N.Y. 1964) (A contract between a brokerage firm and its customer is a contract evidencing a transaction involving commerce within the meaning of the FAA.); *Helca Min. Co. v. Bunker Hill Co.*, 617 P.2d 861 (Idaho 1980) (FAA applied to contract between two mining companies because

applying the FAA. These courts look to the subjective intent of the parties rather than to whether the contract

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contract clearly involved interstate commerce.); *Kodak Min. Co. v. Carrs Fork Corp.*, 669 S.W.2d 917 (Ky. 1984) (A contract was found to involve interstate commerce where the parties were incorporated in different states, arbitrators under the agreement were selected by federal judges from different states, and the leases in question involved interstate commerce.); *Kaufman v. The Chicago Corp.*, 466 N.W.2d 726 (Mich. App. 1991) (Employment contract with member of national stock exchange involves interstate commerce.); *Scanlon v. P&J Enterprises, Inc.*, 451 N.W.2d 616 (Mich.App. 1990) (Transfer of market expertise from Tennessee to Michigan through a franchise agreement was a transaction in interstate commerce.); *Thayer v. American Financial Advisers, Inc.*, 322 N.W.2d 599, 603-604 (Minn. 1982) ("The legislative history indicates that the federal Act was to have a limited application to contracts between merchants for the interstate shipment of goods. Moreover, the language of the federal Act makes it applicable to contracts 'involving commerce' as opposed to contracts 'affecting commerce,' which is the statutory language that Congress normally uses when it seeks to exercise its full powers over commerce. The Act not only uses the narrower language, but also is without any declaration of some national interest to be served or some nationwide comprehensive scheme of regulation to be created."); *Downey v. Christensen*, 825 P.2d 557 (Mont. 1992) (Dealership agreement was contract evidencing interstate commerce.); *compare William Gibson Jr. Inc. v. James Graff Com.*, 780 P.2d 1131 (Mont. 1989) (Where 5% of business was conducted out of state there was sufficient activity to affect interstate commerce under the FAA.); *Dowd v. First Omaha Securities Corp.*, 495 N.W.2d 36 (Neb. 1993) (Written contract to buy and sell securities is contract directly involved in interstate commerce.); *Dean Witter Reynolds, Inc. v. Roven*, 609 P.2d 720 (N.M. 1980) (Contract concerning commodity trading of gold futures is contract involving commerce under the FAA.); *Trombetta v. Conkling*, 586 N.Y.S.2d 461 (Supp. 1992) (Disputes arising out of employment in the securities market involve interstate commerce.); *Episcopal Housing Corporation v. Federal*

affects or involves interstate commerce. The erroneous, restrictive standard originated in the Second Circuit's opinion in *Metro Indust. Painting v. Terminal Const. Co., Inc.*, 287 F.2d 382 (2nd Cir. 1961), *cert. denied*, 368 U.S. 817 (1961), and has not been adopted by any federal circuit court of appeals.

In *Metro* Chief Judge Lumbard, in his concurring opinion, created the restrictive standard stating that a contract involves interstate activity if at the time the parties entered into it and accepted the arbitration clause, they contemplated substantial interstate activity.[3] *Metro*

Insurance Company, 239 S.E.2d 647 (S.C. 1977) (A construction contract evidences transactions in commerce where labor, supplies and materials from all over the country were utilized in the construction.); *Tennessee River Pulp & Paper v. Eichleay*, 637 S.W.2d 853 (Tenn. 1982) (Contract in this case found to evidence a transaction involving interstate commerce where contract exceeded $15,000,000.00 and was between two Delaware corporations; the plaintiff's home office was in Illinois; defendant's home office was in Pennsylvania; the materials used, the labor employed, and the subcontractors involved, in substantial part, came from outside Tennessee; substantial quantities of materials and supplies came from 26 different states; 34% of all materials and supplies were purchased outside of Tennessee.); *International Bank of Commerce v. Caquias*, 846 S.W.2d 496 (Tex.App. – Corpus Christi 1993) (Where loan funds provided under note were derived from interstate financial markets the loan was a transaction involving commerce.); *See also Jack B. Anglin Co., Inc. v. Tipps*, 842 S.W.2d 266 (Tex. 1992); *Kinsey v. Bradley*, 765 P.2d 1329 (Wash.App. 1989) (Commodities account customer agreement involved interstate commerce.); *See also Wineland v. Marketex International, Inc.*, 627 P.2d 967 (Wash.App. 1981); *See also Allison v. Medicab International, Inc.*, 597 P.2d 380 (Wash. 1979).

[3] The majority did not address the issue, stating that irrespective of whether Congress intended the coverage of the FAA

Indust. Painting v. Terminal Const. Co., Inc., 287 F.2d 382, 387 (2nd Cir. 1961). The more restrictive standard was based on a belief that Congress did not intend the scope of the FAA to be applied to the full extent of the commerce power. *Metro*, 287 F.2d at 387. This very premise was rejected by this Court in *Southland Corp. v. Keating*, 465 U.S. 1, 13 (1984), and *Perry v. Thomas*, 482 U.S. 483, 490 (1987). Moreover, the more restrictive standard is

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to be as broad as the constitutional dimensions of the commerce power, the facts found by the judge below were sufficient to support a finding that the transaction evidenced by the contract was within the statutory requirements of the FAA. *Metro Indust. Painting v. Terminal Const. Co., Inc.*, 287 F.2d 382 (2nd Cir. 1961). Moreover, subsequent opinions from the Second Circuit suggest that the *Metro* court did not intend to create a new standard, but was merely attempting to count the contacts between the parties and relevant states to determine whether the contract involved interstate activity. *E.g., Reed & Martin, Inc. v. Westinghouse Elec. Corp.*, 439 F.2d 1268 (2nd Cir. 1971) (within the power of Congress to enact regulations that deal with interstate commerce); *Bartell Media Corp. v. Fawcett Printing Corp.*, 342 F.Supp. 196, 198 (D.C.N.Y. 1972) (Agreement between Delaware magazine publisher and Kentucky printer involved "commerce" within the FAA, where the actual printing of the magazines was accomplished in Kentucky, paper used was shipped from Louisiana, type was set in Pennsylvania, engravings used were made in Tennessee, editorial material was prepared in New York, and printed magazines were shipped to nine states from which they were distributed throughout the U.S.); *United Aircraft Intern., Inc. v. Greenlandair, Inc.*, 298 F.Supp. 1329, 1330 (D.C.Conn. 1969) (Contract for the purchase of helicopters was contract involving "commerce."); *Pennsylvania Engineering Corp. v. Islip Resource Recovery Agency*, 710 F.Supp. 456 (E.D.N.Y. 1989) (Contract clearly "affected" interstate commerce where multimillion dollar construction project built in N.Y. by Delaware corporation involved engineers, contractors, and supplies from many states.).

wholly inconsistent with the very broad and liberal policy favoring arbitration enunciated by this Court in *Prima Paint Corp. v. Flood & Conklin Manufacturing Co.*, 388 U.S. 395, 401 n.7 (1967), *Southland Corp. v. Keating*, 465 U.S. 1, 13 (1984), and *Perry v. Thomas*, 482 U.S. 483, 490 (1987).

The use of the more restrictive standard has increased among the States as a means to limit the applicability of the FAA. In the case of *Allied-Bruce Terminix Companies, Inc., et al. v. Dobson, et al.*, [1920473, August 13, 1993], ___ So. 2d ___ (Ala. 1993), the Supreme Court of Alabama relied exclusively upon the restrictive standard, holding that the FAA applies only when the parties to the contract contemplated, at the time they entered into the contract, substantial interstate activity.

The subjective nature of this test is exaggerated by the inclusion of the "*substantial* interstate activity" requirement. Litigants may easily defeat motions to enforce arbitration clauses by denying that they contemplated "*substantial* interstate activity," since "substantial" is itself a subjective word open to the litigant's own interpretation.

The restrictive standard is also applied in Florida, Georgia, Indiana, Kansas, Massachusetts, Nevada, and North Carolina.[4] Clearly, the adoption of this standard

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[4] *E.g., Acton CATV, Inc. v. Wildwood Partners, Ltd.*, 508 So. 2d 1274 (Fla.App. 5 Dist. 1987) (In determining that an agreement evidences a transaction involving interstate commerce, court should give primary emphasis to intentions of the original contracting parties and original contract itself.); *compare Victor v. Dean Witter Reynolds, Inc.*, 606 So. 2d 681 (Fla.App. 5 Dist.1992); *compare ESAB Automation, Inc. v. Hesco Sales, Inc.*, 582 So. 2d 810

represents a revival of the traditional state hostility towards arbitration that the FAA was specifically intended to eliminate. *See Ex parte Alabama Oxygen*, 433 So. 2d 1158 (Ala. 1983), *vacated and remanded*, 465 U.S. 1016 (1984)(Alabama Supreme Court held that FAA did not preempt state law prohibiting enforcement of arbitration agreements. Reversal by this Court was necessary to overcome Alabama's persistant hostility towards arbitration.).

Until this Court explicitly rejects the "contemplation" test, the number of States adopting the aberrant standard

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(Fla.App. 3 Dist. 1991); *compare United Services General Life Co. v. Bauer*, 568 So. 2d 1321 (Fla.App. 2 Dist. 1990); *Robinson-Humphrey Co., Inc. v. Williams*, 389 S.E.2d 345 (Ga.App. 1989), *cert. denied*, 193 Ga.App. 910 (Customer agreement under which party acting as trustee under related trust agreement agreed to act as broker with respect to funds held in trust, contemplated purchase and sale of securities on national exchanges and therefore involved "transactions involving commerce" within the meaning of the FAA.); *compare DiMambro-Northend Associates v. Blanck-Alvarez, Inc.*, 309 So. 2d 364, 367 (Ga. 1983); *Pathman Const. Co. v. Knox County Hospital Ass'n*, 326 N.E.2d 844 (Ind. 1975) (A contract involves commerce if at the time the contract was executed, the parties contemplated any transaction involving interstate commerce.); *see also University Case Works Systems, Inc. v. Bahre*, 362 N.E.2d 155 (Ind.App. 1977); *R.J. Palmer Const. v. Wichita Band Etc.*, 642 P.2d 127 (Kan.App. 1982) (Parties must contemplate substantial interstate activity.); *Loche v. Dean Witter Reynolds, Inc.*, 526 N.E.2d 1296 (Mass.App.Ct. 1988) (FAA applies when relationship contemplated transaction in interstate commerce.); *Sentry Systems, Inc. v. Guy*, 654 P.2d 1008 (Nev. 1982) (FAA applies where agreement contemplates interstate commerce on its face and evidences a transaction involving commerce.); *Burke County Public Schools Board of Education v. Shaver Partnership*, 279 S.E.2d 816 (N.C. 1981) (Parties must have contemplated substantial interstate activity in the contract.).

as a means to barring enforcement of arbitration agreements may continue to grow. With litigation expenses rising across the United States, arbitration is an increasingly popular alternative for resolving disputes. For arbitration to be effective, however, the enforceability of arbitration agreements must be consistent and uniform throughout every jurisdiction. A statement is needed from this Court establishing conclusively the proper scope of the FAA.

The proper standard for courts to apply in determining whether a contract comes within the provisions of the FAA is whether that contract relates to or affects interstate commerce in any way. Any interstate activity or connection with interstate activity such as a party being from another state, purchase and transportation of materials from another state, or the production of goods within one state for ultimate consumption in another state is sufficient to invoke the coverage of the FAA. The mere fact that the work under a contract is to be performed solely within one state should not prevent the application of the FAA to that contract if the activity under the contract, either through the involvement of parties from other states or through the use of goods from other states, affects or relates to interstate commerce. *Perry v. Thomas*, 482 U.S. 483, 490 (1987); *Southland Corp. v. Keating*, 465 U.S. 1, 13 (1984); *Prima Paint Corp. v. Flood & Conklin Manufacturing Co.*, 388 U.S. 395, 401 (1967); *Mesa Operating Limited Partnership v. Louisiana Intrastate Gas Corp.*, 797 F.2d 238, 243 (5th Cir. 1986); *Snyder v. Smith*, 736 F.2d 409, 417-420 (7th Cir. 1984).

SUMMARY OF THE ARGUMENT

This Court has held that the Federal Arbitration Act applies to the full extent of the power of Congress over interstate commerce. *Perry v. Thomas*, 482 U.S. 483, 490 (1987); *Southland Corp. v. Keating*, 465 U.S. 1, 13 (1984); *Prima Paint Corp. v. Flood & Conklin Manufacturing Co.*, 388 U.S. 395, 401 (1967). The holding of the Supreme Court of Alabama in the case of *Allied-Bruce Terminix Companies, Inc., v. Dobson*, [1920473, August 13, 1993], ___ So. 2d ___ (Ala. 1993), undermines the broad and liberal federal policy favoring the enforceability of arbitration agreements by limiting the application of the Federal Arbitration Act to transactions where the parties actually contemplated, at the time they entered into the contract, substantial interstate activity. The Supreme Court of Alabama's restriction on the application of the Federal Arbitration Act is clearly contrary to the precedent of this Court.

CONCLUSION

For the reasons set forth above, this Court should grant the Petition for a Writ of Certiorari to the Supreme Court of Alabama, reverse the opinion of the Supreme Court of Alabama, and remand for entry of an opinion reversing the trial court's order denying Petitioners'

"Motion to Compel Arbitration and to Stay Litigation Pending Arbitration" filed pursuant to the FAA.

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FILED
MAY 19 1994
OFFICE OF THE CLERK

No. 93-1001

In The Supreme Court of the United States

October Term, 1993

Allied-Bruce Terminix Companies, Inc., and Terminix International Company,
Petitioners,

v.

G. Michael Dobson, Wanda C. Dobson, Steven Gwin and Jan Gwin,
Respondents.

On Writ of Certiorari to the Supreme Court of Alabama

JOINT APPENDIX

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PETITION FOR CERTIORARI FILED DECEMBER 22, 1993
WRIT OF CERTIORARI GRANTED MARCH 21, 1994

107 PP

EDITOR'S NOTE

THE FOLLOWING PAGES WERE POOR HARD COPY AT THE TIME OF FILMING. IF AND WHEN A BETTER COPY CAN BE OBTAINED, A NEW FICHE WILL BE ISSUED.

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DATE	PROCEEDINGS
10/15/91	Complaint filed in CV 91-796
11/26/91	ANSWER (Steven C. Gwin and Jan A. Gwin)
11/26/91	ANSWER OF DEFT TERMINIX INTERNATIONAL COMPANY, L.P. TO PLTFS' COMPLAINT
11/26/91	ANSWER OF DEFT ALLIED-BRUCE TERMINIX COMPANIES, INC. D/B/A TERMINIX SERVICE TO PLTFS' COMPLAINT
12/6/91	ANSWER OF DEFTS STEVEN C. GWIN AND JAN A. GWIN (Amended)
2/14/92	MOTION FOR SUMMARY JUDGMENT
6/25/93	FIRST AMENDED COMPLAINT
6/30/92	MOTION FOR SUMMARY JUDGMENT
7/2/92	MOTION OF DEFT, ALLIED-BRUCE TERMINIX COMPANIES, INC. D/B/A TERMINIX SERVICE AND TERMINIX INTERNATIONAL COMPANY, L.P. TO STRIKE FIRST AMENDED COMPLAINT FILED BY PLTFS
7/2/92	MOTION OF DEFTS, ALLIED-BRUCE TERMINIX COMPANIES, INC. D/B/A TERMINIX SERVICE AND TERMINIX INTERNATIONAL COMPANY, L.P. TO STRIKE CROSS-CLAIM FILED BY DEFTS STEVEN C. GWIN AND JAN A. GWIN
7/6/92	ANSWER OF DEFTS STEVEN C. GWIN AND JAN A. GWIN TO AMENDED COMPLAINT
7/6/92	RESPONSE OF DEFTS, ALLIED-BRUCE TERMINIX COMPANIES, INC. D/B/A TERMINIX SERVICE AND TERMINIX INTERNATIONAL COMPANY, L.P., IN OPPOSITION TO MOTION TO COMPEL FILED BY PLTFS, G. MICHAEL DOBSON AND WANDA C. DOBSON

DATE	PROCEEDINGS
7/31/92	STATEMENT IN OPPOSITION TO MOTION FOR SUMMARY JUDGMENT
8/3/92	MEMORANDUM BRIEF IN OPPOSITION TO MOTION FOR SUMMARY JUDGMENT
8/7/92	DEFT'S REPLY BRIEF IN FURTHER SUPPORT OF THEIR MOTION FOR SUMMARY JUDGMENT
8/14/92	MOTION OF DEFTS, ALLIED-BRUCE TERMINIX COMPANIES, INC. D/B/A TERMINIX SERVICE AND TERMINIX INTERNATIONAL COMPANY, L.P., FOR STAY PENDING ARBITRATION AND FOR ORDER COMPELLING ARBITRATION
8/14/92	AFFIDAVIT OF W. BRUCE ALVERSON IN SUPPORT OF MOTION BY DEFTS, ALLIED-BRUCE TERMINIX COMPANIES, INC. D/B/A TERMINIX SERVICE AND TERMINIX INTERNATIONAL CO. L.P., FOR STAY PENDING ARBITRATION AND FOR ORDER COMPELLING ARBITRATION
8/14/92	AFFIDAVIT OF DANIEL F. JOHNSON IN SUPPORT OF MOTION BY DEFTS, ALLIED-BRUCE TERMINIX COMPANIES, INC., D/B/A TERMINIX SERVICE AND TERMINIX INTERNATIONAL CO., L.P., FOR STAY PENDING ARBITRATION AND FOR ORDER COMPELLING ARBITRATION
8/26/92	Protective Order (copies mailed)
9/1/92	BRIEF OF G. MICHAEL DOBSON AND WANDA C. DOBSON IN OPPOSITION TO MOTION TO COMPEL ARBITRATION
10/27/92	MOTION OF DEFTS, ALLIED-BRUCE TERMINIX COMPANIES, INC., D/B/A TERMINIX SERVICE AND TERMINIX INTERNATIONAL COMPANY, L.P., FOR SEPARATE TRIAL OF CROSS-CLAIM

DATE	PROCEEDINGS
10/28/92	ANSWER OF DEFT TERMINIX INTERNATIONAL COMPANY, L.P., TO PLTFS' FIRST AMENDED COMPLAINT
10/28/92	ANSWER OF DEFT ALLIED-BRUCE TERMINIX COMPANIES, INC. D/B/A TERMINIX SERVICE TO PLTFS' FIRST AMENDED COMPLAINT
10/28/92	ANSWER OF DEFT TERMINIX INTERNATIONAL COMPANY, L.P. TO CROSS-CLAIM OF DEFTS, STEVEN C. GWIN AND JAN A. GWIN
10/28/92	ANSWER OF DEFT ALLIED-BRUCE TERMINIX COMPANIES, INC., D/B/A TERMINIX SERVICE TO CROSS-CLAIM OF DEFTS, STEVEN C. GWIN AND JAN A. GWIN
10/30/92	MOTION OF DEFT, ALLIED-BRUCE TERMINIX COMPANIES, INC., D/B/A TERMINIX SERVICE AND TERMINIX INTERNATIONAL COMPANY, L.P. FOR PARTIAL SUMMARY JUDGMENT
10/30/92	SUMMARY OF DEFTS, ALLIED-BRUCE TERMINIX COMPANIES, INC., D/B/A TERMINIX SERVICE AND TERMINIX INTERNATIONAL COMPANY, L.P., OF UNDISPUTED FACTS OFFERED IN SUPPORT OF MOTION FOR PARTIAL SUMMARY JUDGMENT
11/5/92	OBJECTION TO MOTION FOR SEPARATE TRIAL
11/9/92	BRIEF OF DEFTS, ALLIED-BRUCE TERMINIX COMPANIES, INC. D/B/A TERMINIX SERVICE AND TERMINIX INTERNATIONAL COMPANY, L.P., IN SUPPORT OF THEIR MOTION FOR PARTIAL SUMMARY JUDGMENT
12/14/92	Motion for Order compeling arbitration and for order of stay pending arbitration is denied

DATE	PROCEEDINGS
12/16/92	Notice of Appeal (Supreme Court)
12/16/92	Security for costs
12/16/92	MOTION OF DEFTS, ALLIED-BRUCE TERMINIX COMPANIES, INC., D/B/A TERMINIX SERVICE AND TERMINIX INTERNATIONAL COMPANY, L.P., FOR STAY OF ACTION PENDING APPEAL OF ORDER DENYING MOTION TO STAY PENDING ARBITRATION AND FOR ORDER COMPELLING ARBITRATION
12/22/92	This case is transferred to the administrative docket pending disposition on appeal
12/23/92	Order (to stay) copies mailed
12/23/92	Designation of record on appeal

Form Approved OMB No. 2900-0152

VETERANS ADMINISTRATION
US DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
WOOD DESTROYING INSECT INFORMATION
EXISTING CONSTRUCTION

1A. VA CASE NUMBER	7. DATE
	5/7/91
1B. HUD/FHA CASE NUMBER	

PRIVACY ACT INFORMATION - The information requested on this form will be used in evaluating the property for a VA or HUD insured loan. Although you are not required by law to provide information, failure to provide it can result in rejection of the property as security for your loan. The information collected will not be disclosed outside VA or HUD except as permitted by law. VA and HUD are authorized to request this information by statute *(38 U.S.C., 1810(b)(4) and 12 U.S.C., 1701 et seq.)*

READ THESE INSTRUCTIONS CAREFULLY BEFORE COMPLETING THIS FORM

1. The VA case number or HUD/FHA case number shall be inserted in Item 1 by the lender or the pest control company.
2. When treatment is indicated in Item 8C, the insects treated will be named, the data on application method and chemicals used shall be entered in Item 10. Proper control measures may include issuance of warranty. Warranty information should also be entered below. Proper control measures are those which follow good acceptable industry practices.
3. If visual evidence is found, the insects causing such evidence will be listed in Item 8A and damage resulting from such infestation will be noted in Item 8D.
4. Areas that were inaccessible or obstructed *(Item 7)* may include, but are not limited to, wall covering, fixed ceilings, floor coverings, furniture or stored articles. The Pest Control Operator (PCO) should list, in Item 7, those obstructions or areas which inhibit the inspection.
5. Item 8A may be checked when the PCO is not authorized to perform control measures by the owner/seller or control measures cannot be performed due to conditions beyond control, e.g. obstruction, weather, etc.
6. Visible, evidence of conditions conducive to infestation from subterranean termites shall be reported on reverse of the form *(earth-wood contact, faulty grades, insufficient ventilation, etc.)*.

3A. NAME OF INSPECTION COMPANY	5A. NAME OF PROPERTY OWNER/SELLER
Terminix Service	Steven Gwin
3B. ADDRESS OF INSPECTION COMPANY *(Include ZIP Code)*	**5B. ADDRESS OF PROPERTY**
P O Box 1830 Daphne, Al. 36526	114 Fels Ave Fairhope, Al. 36532
3C. TELEPHONE NUMBER *(Include Area Code)*	**4. PEST CONTROL OPERATOR LICENSE NUMBER**
205/928-5502	1002
	5C. STRUCTURE(S) INSPECTED
	Residence

FINDINGS

6. WERE ANY AREAS OF THE PROPERTY OBSTRUCTED OR INACCESSIBLE?	7. OBSTRUCTIONS OR INACCESSIBLE AREAS *(specify)* *(Read Item 11B before completing.)*
☒ Yes ☐ No *(If "Yes" complete Item 7)*	Behind interior and exterior wall coverings and under floor coverings.

8. BASED ON CAREFUL VISUAL INSPECTION OF THE READILY ACCESSIBLE AREAS OF THE PROPERTY *(See Item 11A before completing).*

☐ A. Visible evidence of wood destroying insects was observed. No control measures were performed. Insects observed:

☐ B. No visible evidence of infestation from wood destroying insects was observed.

☐ C. Visible evidence of infestation was noted; proper control measures were performed.

☒ D. Visible damage due to Subterranean Termites has been observed in the following areas: SEE ATTACHED GRAPH

☐ E. Visible evidence of previously treated infestation, which is now inactive, was observed. *(Explain in Item 10.)*

9. DAMAGE OBSERVED ABOVE, IF ANY. *(Check One)*	10. ADDITIONAL COMMENTS *(If necessary, continue on reverse.)*
☐ A. Will be/has been corrected by this company. ☐ B. Will be corrected by another company *(see attached contract)*. ☒ C. Will not be corrected by this company. Recommend that damage be evaluated by qualified building expert.	

11. STATEMENT OF PEST CONTROL OPERATOR

A. The inspection covered the readily accessible areas of the property, including attics and crawl spaces which permit entry. Special attention was given to those accessible areas which experience has shown to be particularly susceptible to attack by wood destroying insects. Probing and/or sounding of those areas and other visible accessible wood members showing evidence of infestation was performed.

B. The inspection did not include areas which were obstructed or inaccessible at the time of inspection. *(See instruction number 4 above.)*

C. This is not a structural damage report. Neither is this a warranty as to absence of wood destroying insects.

D. Neither I nor the company for which I am acting have had, presently have, or contemplate having any interest in the property. I do further state that neither I nor the company for which I am acting is associated in any way with any party to this transaction.

12A. SIGNATURE OF AUTHORIZED COMPANY REPRESENTATIVE	12B. TITLE	12C. DATE
John Buck	INSPECTOR	5/7/91

STATEMENT OF PURCHASER

I have received the original or a legible copy of this form.

14. SIGNATURE OF PURCHASER	15. DATE
S. Michael Dobson Wanda C. Dobson	5/10/91

VA FORM 26-8850
HUD 92053 (APR 1983)

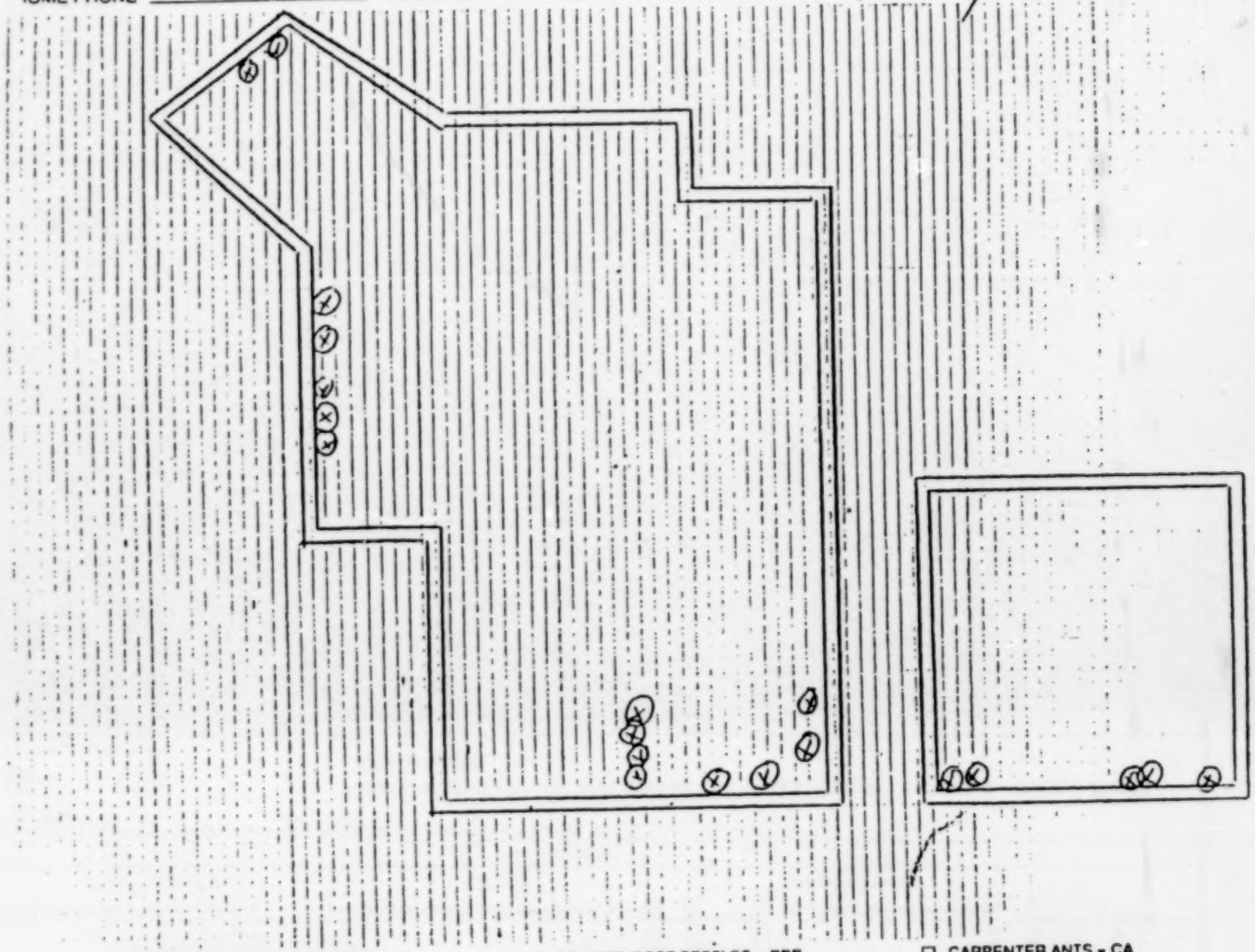
TERMINIX INSPECTION GRAPH

153

OWNER'S NAME Steven Gwin OCCUPANT _____ DATE 5-7-91

TREATING ADDRESS 114 Fels Ave CITY Fairhope STATE AL. ZIP 36532

HOME PHONE _____ BUSINESS PHONE _____ INSPECTED BY John Burk



KEY:
- ☐ SUBTERRANEAN TERMITES = XXX
- ☐ DRYWOOD TERMITES = KKK
- ☐ DAMPWOOD TERMITES = ZZZ
- ☐ EXISTING DAMAGE = ⊗
- ☐ POWDER-POST BEETLES = PPB
- ☐ WOOD BORING BEETLES = WB
- ☐ FUNGUS = F
- ☐ WELL/CISTERN = W/C
- ☐ CARPENTER ANTS = CA
- ☐ CELLULOSE DEBRIS = CD
- ☐ EXCESSIVE MOISTURE = EM
- ☐ FAULTY GRADE = FG
- ☐ EARTH-WOOD CONTACTS = EC

TYPE OF CONSTRUCTION: ☑ CRAWL SPACE ☐ BASEMENT ☐ MONOLITHIC SLAB ☑ FLOATING SLAB ☐ SUPPORTED SLAB

TYPE OF FOUNDATION: ☐ CONCRETE ☑ HOLLOW BLOCK ☐ BRICK ☐ STONE ☐ OTHER _____

PROPERTY HAS A: 1. WELL ☐ YES ☐ NO 2. CISTERN ☐ YES ☐ NO 3. SUMP PUMP ☐ YES ☐ NO 4. FRENCH DRAIN ☐ YES ☐ NO

INSPECTOR'S STATEMENT OF VISIBLE DAMAGE

OLD TERMITE AND MOISTURE DAMAGE TO UNDERNEATH OF STRUCTURES AS MARKED ON GRAPH

BY: John Burk DATE: 5-7-91

CONTROL TECHNICIAN'S STATEMENT OF VISIBLE DAMAGE

BY: _____ DATE: _____

TERMINIX IS NOT RESPONSIBLE FOR REPAIRS TO DAMAGES DISCLOSED ABOVE IN ADDITION, HIDDEN DAMAGE MAY EXIST IN CONCEALED OR INACCESSIBLE AREAS. TERMINIX CANNOT GUARANTEE THAT THE DAMAGE DISCLOSED BY VISUAL INSPECTION OF THE PREMISES SHOWN ABOVE REPRESENTS THE ENTIRETY OF THE DAMAGE WHICH MAY EXIST AS OF THE DATE OF THE INITIAL CONTROL APPLICATION. TERMINIX SHALL NOT BE RESPONSIBLE FOR REPAIR OF ANY EXISTING DAMAGE, INCLUDING WITHOUT LIMITATION ANY DAMAGE WHICH EXISTED IN AREAS OR IN STRUCTURAL MEMBERS WHICH WERE NOT ACCESSIBLE FOR VISUAL INSPECTION AS OF THE DATE OF THIS GRAPH.

THE ABOVE GRAPH, AND THE AREAS CONTAINING VISIBLE ACTIVITY OR DAMAGE, HAVE BEEN DESCRIBED TO ME, AND ARE AFFIRMED BY ME AS OWNER OR AGENT OF THE ABOVE PROPERTY. I ALSO AFFIRM THAT I UNDERSTAND THAT TERMINIX IS NOT LIABLE FOR HIDDEN DAMAGE INACCESSIBLE TO THE INSPECTOR.

DATE: _____ BY: _____

FORM #33021 REV 1/90
© 1987 The Terminix International Company L.P.

IN THE CIRCUIT COURT
OF BALDWIN COUNTY, ALABAMA

Case No. CV-91-796

G. MICHAEL DOBSON and WANDA C. DOBSON,
Plaintiffs,

VS.

THE TERMINIX INTERNATIONAL COMPANY, L.P.,
TERMINIX SERVICE, STEVEN C. GWIN, and JAN A. GWIN,
Defendants.

COMPLAINT

[Filed Oct. 15, 1991]

COUNT ONE

Come now the Plaintiffs in the above styled cause and claim damages of the Defendants and as grounds therefor would show unto the Court as follows:

1. That on or about May 10, 1991, the Plaintiffs did purchase from the Defendants, Steven C. Gwin and Jan A. Gwin (hereinafter referred to as "Gwin"), a residential dwelling house located at 114 Fels Avenue in the City of Fairhope, Baldwin County, Alabama.

2. That prior to said date, the Defendants, Gwin, either acting personally or through their agent, Frankie Evans, represented to the Plaintiffs that any termite damage suffered by said dwelling house consisted of "old" damage and that the same had been repaired, all termites treated and that there existed no live infestation of termites in said dwelling; that a new roof had been erected

on said dwelling and that the same did not leak and was in good condition; and that the electrical wiring in said dwelling was in good condition.

3. That prior to said date, the Defendants, Terminix International Company, L.P. and Terminix Service (hereinafter referred to as "Terminix"), undertook to inspect said dwelling for the purpose of determining the existence of any wood destroying insects and that said Defendants represented to the Plaintiffs that there was no visible evidence of infestation from wood destroying insects.

4. That all of said representations were false in that said dwelling was infested throughout with live termites, of which there was visible evidence; that the roof was damaged, leaking and had not been replaced; and that the electrical wiring was defective and in violation of local and national electrical codes.

5. That said misrepresentations were of material facts and were made by the Defendants, either willfully to deceive; recklessly without knowledge; or by mistake and innocently, but, in any event, constitute legal fraud as that term is defined by *Code of Alabama*, Section 6-5-101, et seq. (1975).

6. That the Plaintiffs relied on said misrepresentations to their detriment in that they purchased said dwelling house believing the truth of the representations made to them.

7. That as a proximate result of said misrepresentations, the Plaintiffs have been damaged in that they have been required to retain substitute housing while repairs have been made to the dwelling which they purchased; that portions of their dwelling remain damaged from said infestation; that they have been caused to suffer mental anguish; and that their dwelling has been rendered less valuable because of the fear of future termite infestations.

WHEREFORE, Plaintiffs demand judgment against the Defendants for such damages to which they might be

entitled, in excess of the jurisdiction of this Court, together with interest and costs.

COUNT TWO

Come now the Plaintiffs in the above styled cause and claim damages of the Defendants, Terminix International Company, L.P. and Terminix Service, and as grounds therefor would show unto the Court as follows:

1. Plaintiffs adopt and incorporate herein paragraphs one and three of Count One of the Complaint.

2. That in the event the Defendants, Terminix, did not have actual knowledge of the existence of wood destroying insects in said dwelling, then in such event the inspection undertaken by the Defendants, Terminix, was done in a negligent or wanton manner.

3. That as a proximate result of said negligence or wantonness of the Defendants, Terminix, the Plaintiffs have been damaged in that they have been required to retain substitute housing while repairs have been made to the dwelling which they purchased; that portions of their dwelling remain damaged from said infestation; they have been caused to suffer mental anguish; and the dwelling which they purchased has been rendered less valuable because of the fear of future termite infestation.

WHEREFORE, Plaintiffs demand judgment against the Defendants, Terminix, for such damages to which they might be entitled, in excess of the jurisdiction of this Court, together with interest and costs.

COUNT THREE

Come now the Plaintiffs in the above styled cause and claim damages of the Defendants, Gwin, and as grounds therefor would show unto the Court as follows:

1. Plaintiffs herein adopt and reallege the allegations of paragraph one of Count One of the Complaint.

2. That prior to said date, the said dwelling was infested throughout with live termites; the roof was dam-

aged, leaking and had not been replaced; and the electrical wiring was defective and in violation of local and national electrical codes.

3. That the Plaintiffs were not aware of said conditions prior to the purchase of said dwelling because the same were fraudulently concealed from them by the Defendants, Gwin.

4. That as a proximate cause of said fraudulent concealment, the Plaintiffs were prevented from discovering the existence of said material facts and were thereby induced to purchase said dwelling to their detriment and as a proximate result thereof have been damaged in that they have been required to retain substitute housing while repairs have been made to the dwelling which they purchased; that portions of their dwelling remain damaged from said infestation; they have been caused to suffer mental anguish; and their dwelling has been rendered less valuable because of the fear of future termite infestations.

WHEREFORE, Plaintiffs demand judgment against Defendants, Gwin, for such damages to which they might be entitled, in excess of the jurisdiction of this Court, together with interest and costs.

/s/ Allan R. Chason
ALLAN R. CHASON
Attorney for Plaintiffs

Of Counsel:

CHASON & CHASON, P.C.
P. O. Box 100
Bay Minette, Alabama 36507

Plaintiffs respectfully request a trial by jury of all issues stated in the foregoing Complaint.

/s/ Allan R. Chason
ALLAN R. CHASON
Attorney for Plaintiffs

[Service by Certified Mail Omitted in Printing]

IN THE CIRCUIT COURT
OF BALDWIN COUNTY, ALABAMA

[Title Omitted in Printing]

ANSWER OF DEFENDANT TERMINIX INTERNATIONAL COMPANY, L.P. TO PLAINTIFFS' COMPLAINT

[Filed Nov. 26, 1991]

COMES NOW, Terminix International Company, L.P. (hereinafter referred to as "Terminix International"), a Defendant in the above-styled action, and answers the numbered paragraphs of Plaintiffs' complaint as follows:

COUNT ONE

1. Defendant Terminix International is without knowledge or information sufficient to form a belief as to the truth of the allegations contained in paragraphs 1 through 2 of Count One of Plaintiffs' complaint and thus, denies the same and demands strict proof thereof.

2. Defendant Terminix International denies the allegations of paragraphs 3 through 7 of Count One of Plaintiffs' complaint and demands strict proof thereof.

COUNT TWO

3. Answering paragraph 1 of Count Two of Plaintiffs' complaint, Defendant Terminix International incorporates by reference paragraphs 1 and 2 of this answer as if the same had been set forth in full herein.

4. Defendant Terminix International denies the allegations of paragraphs 2 through 3 of Count Two of Plaintiffs' complaint and demands strict proof thereof.

COUNT THREE

5. The averments contained in paragraphs 1 through 4 of Count Three of Plaintiffs' complaint need not be admitted or denied by Defendant Terminix International, since they relate solely to other Defendants, but inasmuch as said allegations can be construed to require a response from Defendant Terminix International, Defendant Terminix International is without knowledge or information sufficient to form a belief as to the truth of the allegations contained in paragraphs 1 through 4 of Count Three of Plaintiffs' complaint, thus, denies the same and demands strict proof thereof.

6. Any allegation contained in Plaintiffs' complaint which is not hereinbefore admitted is hereby specifically denied.

7. Defendant Terminix International denies that Plaintiffs are entitled to any judgment or relief as requested in their complaint and demands strict proof thereof.

FIRST AFFIRMATIVE DEFENSE

Said complaint and each cause of action contained therein, jointly and separately, fails to state a claim against Defendant Terminix International upon which relief can be granted.

SECOND AFFIRMATIVE DEFENSE

As a second, separate and affirmative defense, Defendant Terminix International asserts that there were one or more sufficient intervening causes which proximately contributed to the damage of which Plaintiffs are complaining; hence, Plaintiffs ought not recover from Defendant Terminix International.

THIRD AFFIRMATIVE DEFENSE

As a third, separate and affirmative defense, Defendant Terminix International asserts that Plaintiffs should not

recover from Defendant Terminix International because Plaintiffs or one or more persons (other than Defendant Terminix International) are guilty of negligence, or other willful, wanton or reckless conduct, which proximately contributed to the damages alleged in Plaintiffs' complaint.

FOURTH AFFIRMATIVE DEFENSE

As a fourth, separate and affirmative defense, Defendant Terminix International asserts that there is no duty owing from said Defendant to Plaintiffs sufficient to support a claim for negligence and/or wantonness.

FIFTH AFFIRMATIVE DEFENSE

As a fifth, separate and affirmative defense, Defendant Terminix International asserts that Plaintiffs have failed to allege with sufficient particularity, the facts constituting a cause of action for fraud.

SIXTH AFFIRMATIVE DEFENSE

As a sixth, separate and affirmative defense, Defendant Terminix International asserts that there was no causal relationship between any alleged breach of a duty by Defendant Terminix International and the damages complained of by Plaintiffs.

SEVENTH AFFIRMATIVE DEFENSE

As a seventh, separate and affirmative defense, Defendant Terminix International asserts that Plaintiffs seek punitive damages in violation of the Excess Fines Clause of the Eighth Amendment of the Constitution of the United States.

EIGHTH AFFIRMATIVE DEFENSE

As a eighth, separate and affirmative defense, Defendant Terminix International asserts that Plaintiffs seek punitive damages in violation of the Due Process Clause

of the Fourteenth Amendment of the Constitution of the United States in one or more of the following respects:

1. The punitive damage claims are vastly disproportionate to the actual damages.
2. The award of punitive damages would constitute an arbitrary and capricious taking of the property of Defendant Terminix International, a taking which is unjustified by any rational state purpose.
3. The award of punitive damages with wholly standardless discretion is inconsistent with due process.

NINTH AFFIRMATIVE DEFENSE

As a ninth, separate and affirmative defense, Defendant Terminix International asserts that the award of punitive damages claimed by Plaintiffs would violate the Fourth, Fifth, Sixth, Eighth and Fourteenth Amendments, separately, of the Constitution of the United States and Article I, Sections 1, 6, 15 and 22 of the Constitution of Alabama, on each of the following separate and several grounds:

1. The procedures may result in the award of joint and several judgments against multiple defendants for different alleged acts of wrongdoing.
2. The procedures fail to provide means for awarding separate judgments against alleged joint tort feasors.
3. The procedures fail to provide a limit on the amount of the award against Defendant Terminix International.
4. The procedures fail to provide specific standards for the award of punitive damages.
5. The procedures fail to provide specific standards for the amount of the award of punitive damages.

6. The procedures permit the award of punitive damages upon satisfaction of a standard of proof less than that applicable to the imposition of criminal sanctions.
7. The procedures permit multiple awards of punitive damage for the same alleged act.
8. The procedures fail to provide a clear consistent appellate standard of review for an award of punitive damages.
9. The procedure may permit the admission of evidence relative to punitive damages in the same proceeding during which liability is determined.
10. The standards of conduct upon which punitive damages are sought are vague.
11. An award of punitive damages as claimed would violate Defendant Terminix International's right to the equal protection of the laws.
12. The award of punitive or extra-contractual damages on the basis of vicarious liability for the conduct of other violates the Fifth, Eighth and Fourteenth Amendments of the United States Constitution as well as the Alabama Constitutional provisions set forth above.
13. It is improper and unconstitutional to assess punitive damages based on derivative or attributed liability, such as respondeat superior liability.

TENTH AFFIRMATIVE DEFENSE

As a tenth, separate and affirmative defense, Defendant Terminix International asserts that the imposition of punitive damages in this case would violate the equal protection clause of the Fifth and Fourteenth Amendments to the United States Constitution, separately, and would deprive Defendant Terminix International of the right to equal protection under the law as provided in

Article I, Sections 1, 6 and 22 of the Alabama Constitution of 1901 because, among other reasons, criminal defendants are placed in a position of distinct advantage over civil defendants of comparable culpability due to the disparity in punitive treatment for similar conduct and because the absence of sufficiently specific and objective standards for the imposition of punitive damages fails to ensure equality of treatment between and among similarly situated civil defendants in the same or in different cases.

ELEVENTH AFFIRMATIVE DEFENSE

As an eleventh, separate and affirmative defense, Defendant Terminix International asserts that present Alabama procedures pursuant to which punitive damages are awarded permit the imposition of punitive damages in excess of the maximum criminal fine for the same or similar conduct, which thereby infringes upon the due process and equal protection provisions of the Alabama and United States Constitutions.

TWELFTH AFFIRMATIVE DEFENSE

As a twelfth, separate and affirmative defense, Defendant Terminix International asserts that the procedures pursuant to which punitive damages are awarded permit the imposition of an excessive fine in violation of the Eighth Amendment of the United States Constitution and Article I, Section 15 of the Alabama Constitution.

THIRTEENTH AFFIRMATIVE DEFENSE

As a thirteenth, separate and affirmative defense, Defendant Terminix International asserts that the award of punitive damages against Defendant Terminix International in this action would violate the prohibition against laws that impair the obligations of contracts in violation of Article I, Section 22 of the Constitution of Alabama.

FOURTEENTH AFFIRMATIVE DEFENSE

As a fourteenth, separate and affirmative defense, Defendant Terminix International asserts that Plaintiffs' demand for punitive damages violates the self-incrimination clauses of the Fifth Amendment of the United States Constitution and of Article I, Section 6 of the Alabama Constitution in that the damages claimed are penal in nature while Defendant Terminix International is required to disclose documents and/or other evidence without the safeguards against self-incrimination set out in the Fifth Amendment.

FIFTEENTH AFFIRMATIVE DEFENSE

As a fifteenth, separate and affirmative defense, Defendant Terminix International asserts that Plaintiffs' demand for punitive damages violates the Sixth Amendment of the United States Constitution in that the Plaintiffs' claim for punitive damages is a claim that is penal in nature, entitling Defendant Terminix International to the same procedural safeguards accorded to a criminal defendant under the Sixth Amendment.

SIXTEENTH AFFIRMATIVE DEFENSE

As a sixteenth, separate and affirmative defense, Defendant Terminix International asserts that Plaintiffs' demand for punitive damages violates the Fifth Amendment of the United States Constitution and violates Article I, Section 6 of the Alabama Constitution in that no person shall be deprived of life, liberty or property except by due process of law and the punitive damages claimed are vague and not rationally related to any legitimate government interests.

SEVENTEENTH AFFIRMATIVE DEFENSE

As a seventeenth, separate and affirmative defense, Defendant Terminix International asserts that Plaintiffs' complaint is due to be dismissed as to said Defendant due to insufficiency of service of process.

/s/ Joseph P. Jones, Jr.
JOSEPH P. JONES, JR.
T. JULIAN MOTES
Attorneys for Defendant
Terminix International
Company, L.P.

Of Counsel:

SIROTE & PERMUTT, P.C.
One St. Louis Centre, Suite 1000
Post Office Drawer 2025
Mobile, Alabama 36652
(205) 432-1671

[Certificate of Service Omitted in Printing]

IN THE CIRCUIT COURT
OF BALDWIN COUNTY, ALABAMA

(Title Omitted in Printing)

ANSWER OF DEFENDANT ALLIED-BRUCE TERMINIX COMPANIES, INC., D/B/A TERMINIX SERVICE TO PLAINTIFFS' COMPLAINT

[Filed Nov. 26, 1991]

COMES NOW, Allied-Bruce Terminix Companies, Inc., d/b/a Terminix Service (hereinafter referred to as "Terminix Service"), a Defendant in the above-styled action, and answers the numbered paragraphs of Plaintiffs' complaint as follows:

COUNT ONE

1. Defendant Terminix Service is without knowledge or information sufficient to form a belief as to the truth of the allegations contained in paragraphs 1 through 2 of Count One of Plaintiffs' complaint and thus, denies the same and demands strict proof thereof.

2. Answering paragraph 3 of Count One of Plaintiffs' complaint, Defendant Terminix Service admits that said Defendant performed a visual inspection of the readily accessible areas of the property involved in this suit on behalf of Defendants, Steven C. Gwin and Jan A. Gwin, and that Defendant Terminix Service submitted a written report on the visual inspection providing, among other things, no visible evidence of infestation from wood destroying insects was observed and visible damage due to subterranean termites has been observed in areas marked on an attached graph. Except as hereinabove already admitted, Defendant Terminix Service denies each

and every remaining allegation contained in paragraph 3 of Count One of Plaintiffs' complaint and demands strict proof thereof.

3. Defendant Terminix Service denies the allegations of paragraphs 4 through 7 of Count One of Plaintiffs' complaint and demands strict proof thereof.

COUNT TWO

4. Answering paragraph 1 of Count Two of Plaintiffs' complaint, Defendant Terminix Service incorporates by reference paragraphs 1 and 2 of this answer as if the same had been set forth in full herein.

5. Answering paragraph 2 of Count Two of Plaintiffs' complaint, Defendant Terminix Service admits that said Defendant during a visual inspection performed on behalf of Defendants, Steven C. Gwin and Jan A. Gwin, of the readily accessible areas of the property involved in this suit observed no visible evidence of infestation from wood destroying insects, but did observe and report visible damage due to subterranean termites. Except as hereinabove already admitted, Defendant Terminix Service denies each and every remaining allegation contained in paragraph 2 of Count Two of Plaintiffs' complaint and demands strict proof thereof.

6. Defendant Terminix Service denies the allegations of paragraph 3 of Count Two of Plaintiffs' complaint and demands strict proof thereof.

COUNT THREE

7. The averments contained in paragraphs 1 through 4 of Count Three of Plaintiffs' complaint need not be admitted or denied by Defendant Terminix Service, since they relate solely to other Defendants, but inasmuch as said allegations can be construed to require a response from Defendant Terminix Service, Defendant Terminix Service is without knowledge or information sufficient to

form a belief as to the truth of the allegations contained in paragraphs 1 through 4 of Count Three of Plaintiffs' complaint, thus, denies the same and demands strict proof thereof.

8. Any allegation contained in Plaintiffs' complaint which is not hereinbefore admitted is hereby specifically denied.

9. Defendant Terminix Service denies that Plaintiffs are entitled to any judgment or relief as requested in their complaint and demands strict proof thereof.

FIRST AFFIRMATIVE DEFENSE

Said complaint and each cause of action contained therein, jointly and separately, fails to state a claim against Defendant Terminix Service upon which relief can be granted.

SECOND AFFIRMATIVE DEFENSE

As a second, separate and affirmative defense, Defendant Terminix Service asserts that there were one or more sufficient intervening causes which proximately contributed to the damage of which Plaintiffs are complaining; hence, Plaintiffs ought not recover from Defendant Terminix Service.

THIRD AFFIRMATIVE DEFENSE

As a third, separate and affirmative defense, Defendant Terminix Service asserts that Plaintiffs should not recover from Defendant Terminix Service because Plaintiffs or one or more persons (other than Defendant Terminix Service) are guilty of negligence, or other willful, wanton or reckless conduct, which proximately contributed to the damages alleged in Plaintiffs' complaint.

FOURTH AFFIRMATIVE DEFENSE

As a fourth, separate and affirmative defense, Defendant Terminix Service asserts that there is no duty owing from said Defendant to Plaintiffs sufficient to support a claim for negligence and/or wantonness.

FIFTH AFFIRMATIVE DEFENSE

As a fifth, separate and affirmative defense, Defendant Terminix Service asserts that Plaintiffs have failed to allege with sufficient particularity, the facts constituting a cause of action for fraud.

SIXTH AFFIRMATIVE DEFENSE

As a sixth, separate and affirmative defense, Defendant Terminix Service asserts that there was no causal relationship between any alleged breach of a duty by Defendant Terminix Service and the damages complained of by Plaintiffs.

SEVENTH AFFIRMATIVE DEFENSE

As a seventh, separate and affirmative defense, Defendant Terminix Service asserts that Plaintiffs seek punitive damages in violation of the Excess Fines Clause of the Eighth Amendment of the Constitution of the United States.

EIGHTH AFFIRMATIVE DEFENSE

As a eighth, separate and affirmative defense, Defendant Terminix Service asserts that Plaintiffs seek punitive damages in violation of the Due Process Clause of the Fourteenth Amendment of the Constitution of the United States in one or more of the following respects:

1. The punitive damage claims are vastly disproportionate to the actual damages.
2. The award of punitive damages would constitute an arbitrary and capricious taking of the property of Defendant Terminix Service, a taking which is unjustified by any rational state purpose.
3. The award of punitive damages with wholly standardless discretion is inconsistent with due process.

NINTH AFFIRMATIVE DEFENSE

As a ninth, separate and affirmative defense, Defendant Terminix Service asserts that the award of punitive damages claimed by Plaintiffs would violate the Fourth, Fifth, Sixth, Eighth and Fourteenth Amendments, separately, of the Constitution of the United States and Article I, Sections 1, 6, 15 and 22 of the Constitution of Alabama, on each of the following separate and several grounds:

1. The procedures may result in the award of joint and several judgments against multiple defendants for different alleged acts of wrongdoing.
2. The procedures fail to provide means for awarding separate judgments against alleged joint tort feasors.
3. The procedures fail to provide a limit on the amount of the award against Defendant Terminix Service.
4. The procedures fail to provide specific standards for the award of punitive damages.
5. The procedures fail to provide specific standards for the amount of the award of punitive damages.
6. The procedures permit the award of punitive damages upon satisfaction of a standard of proof less than that applicable to the imposition of criminal sanctions.
7. The procedures permit multiple awards of punitive damage for the same alleged act.

8. The procedures fail to provide a clear consistent appellate standard of review for an award of punitive damages.

9. The procedure may permit the admission of evidence relative to punitive damages in the same proceeding during which liability is determined.

10. The standards of conduct upon which punitive damages are sought are vague.

11. An award of punitive damages as claimed would violate Defendant Terminix Service's right to the equal protection of the laws.

12. The award of punitive or extra-contractual damages on the basis of vicarious liability for the conduct of other violates the Fifth, Eighth and Fourteenth Amendments of the United States Constitution as well as the Alabama Constitutional provisions set forth above.

13. It is improper and unconstitutional to assess punitive damages based on derivative or attributed liability, such as respondeat superior liability.

TENTH AFFIRMATIVE DEFENSE

As a tenth, separate and affirmative defense, Defendant Terminix Service asserts that the imposition of punitive damages in this case would violate the equal protection clause of the Fifth and Fourteenth Amendments to the United States Constitution, separately, and would deprive Defendant Terminix Service of the right to equal protection under the law as provided in Article I, Sections 1, 6 and 22 of the Alabama Constitution of 1901 because, among other reasons, criminal defendants are placed in a position of distinct advantage over civil defendants of comparable culpability due to the disparity in punitive treatment for similar conduct and because the absence of sufficiently specific and objective standards for the imposition of punitive damages fails to ensure equality of

treatment between and among similarly situated civil defendants in the same or in different cases.

ELEVENTH AFFIRMATIVE DEFENSE

As an eleventh, separate and affirmative defense, Defendant Terminix Service asserts that present Alabama procedures pursuant to which punitive damages are awarded permit the imposition of punitive damages in excess of the maximum criminal fine for the same or similar conduct, which thereby infringes upon the due process and equal protection provisions of the Alabama and United States Constitutions.

TWELFTH AFFIRMATIVE DEFENSE

As a twelfth, separate and affirmative defense, Defendant Terminix Service asserts that the procedures pursuant to which punitive damages are awarded permit the imposition of an excessive fine in violation of the Eighth Amendment of the United States Constitution and Article I, Section 15 of the Alabama Constitution.

THIRTEENTH AFFIRMATIVE DEFENSE

As a thirteenth, separate and affirmative defense, Defendant Terminix Service asserts that the award of punitive damages against Defendant Terminix Service in this action would violate the prohibition against laws that impair the obligations of contracts in violation of Article I, Section 22 of the Constitution of Alabama.

FOURTEENTH AFFIRMATIVE DEFENSE

As a fourteenth, separate and affirmative defense, Defendant Terminix Service asserts that Plaintiffs' demand for punitive damages violates the self-incrimination clauses of the Fifth Amendment of the United States Constitution and of Article I. Section 6 of the Alabama Constitution in that the damages claimed are penal in nature while Defendant Terminix Service is required to disclose

documents and/or other evidence without the safeguards against self-incrimination set out in the Fifth Amendment.

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As a fifteenth, separate and affirmative defense, Defendant Terminix Service asserts that Plaintiffs' demand for punitive damages violates the Sixth Amendment of the United States Constitution in that the Plaintiffs' claim for punitive damages is a claim that is penal in nature, entitling Defendant Terminix Service to the same procedural safeguards accorded to a criminal defendant under the Sixth Amendment.

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As a sixteenth, separate and affirmative defense, Defendant Terminix Service asserts that Plaintiffs' demand for punitive damages violates the Fifth Amendment of the United States Constitution and violates Article I, Section 6 of the Alabama Constitution in that no person shall be deprived of life, liberty or property except by due process of law and the punitive damages claimed are vague and not rationally related to any legitimate government interests.

/s/ T. Julian Motes
JOSEPH P. JONES, JR.
T. JULIAN MOTES
Attorneys for Defendant
Allied-Bruce Terminix
Companies, Inc., d/b/a
Terminix Service

Of Counsel:

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One St. Louis Centre, Suite 1000
Post Office Drawer 2025
Mobile, Alabama 36652
(205) 432-1671

(Certificate of Service Omitted in Printing)

IN THE CIRCUIT COURT
FOR THE TWENTY-EIGHTH JUDICIAL CIRCUIT
OF ALABAMA
BALDWIN COUNTY

Civil Action Number CV-91-796

C. MICHAEL DOBSON and WANDA C. DOBSON,
Plaintiffs,

VS.

THE TERMINIX INTERNATIONAL COMPANY, L.P.,
TERMINIX SERVICE, STEVEN C. GWIN, and
JAN A. GWIN,
Defendants.

Civil Action Number CV-92-197

STATE FARM FIRE & CASUALTY CO.,
Plaintiff,

VS.

STEVEN C. GWIN, JAN A. GWIN, G. MICHAEL DOBSON,
and WANDA C. DOBSON,
Defendants.

The testimony of WANDA C. DOBSON, taken at the Law Offices of Sirote & Permutt, One St. Louis Centre, 1 St. Louis Street, Suite 1000, Mobile, Alabama, on the 18th day of May, 1992, commencing at approximately 10:15 o'clock, a.m.

Jubilee Grid Systems
19200 County Road33
Fairhope, Al. 36532

Billed to: Terminex
Mike Dobson
114 Fels

DESCRIPTION OF WHAT WORK WAS PERFORMED IN AREAS LISTED BELOW

LIVING ROOM:

Floor Joist - Replace
North Wall - Replace Studs, Siding, Sheetrock & Trim
West Wall - Replace Studs, Siding, Sheetrock & Trim
Ceiling - Replace Sheetrock
Roof - Replace Rafters, Plywood & Shingles

BAY ROOM:

Floor Joist - Replace
North Wall - Replace Studs, Siding, Sheetrock & Trim
East Wall - Replace Studs, Siding, Sheetrock & Trim
Ceiling - Replace Ceiling Joist, Sheetrock

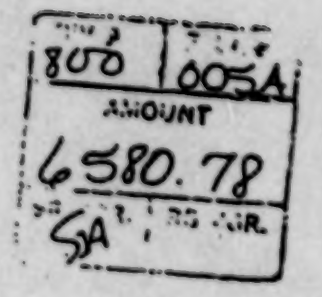
BREAKFAST ROOM:

South, East and West Wall Repaired with Sheetrock

GARAGE & APARTMENT:

South Wall - Replace Studs, Paneling, Sheetrock & Trim
Roof - Replace Rafters, Plywood & Shingles
Ceiling - Replace Sheetrock

Cost of Materials-
5,180.78
Labor-
5,900.00
Total-
11,080.78



DEFENDANT'S EXHIBIT
14

IN THE CIRCUIT COURT
FOR THE TWENTY-EIGHTH JUDICIAL CIRCUIT
OF ALABAMA
BALDWIN COUNTY

(Title Omitted in Printing)

The testimony of G. MICHAEL DOBSON, taken at the Law Offices of Sirote & Permutt, One St. Louis Centre, 1 St. Louis Street, Suite 1000, Mobile, Alabama, on the 19th day of May, 1992, commencing at approximately 8:35 o'clock, a.m.

* * * *

[907] Q Now, you've identified there was basically four phases of the repairs. Can you identify the other three phases for me?

A Yeah, I'll try do to do that and I'll try to do it—if I can flip through this and refresh my memory?

Q Sure. No problem.

A The phase one or what I refer to as phase one, for lack of a better term, included the inside repairs to the bay area, and maybe if I looked on a graph it would help more than looking at this.

Q You're looking at the second page of Defendant's Exhibit 6?

A That's correct.

Q All right.

A And at that point the sheetrock was replaced in this breakfast area.

Q Would that be the only thing done in phase one, as you understood it?

A No. Phase one also included this work done in the photographs that are like 33-A, B and C and many, many others.

Q Okay.

[908] A Where the entire portion of the house, this southwest corner, the entire north side of the house, this (Indicating) west portion of the sunroom, I think we called it yesterday, that was in phase one.

Q Okay. And this conversation that—

A But phase one also continues.

Q Okay. I'm sorry. Go ahead and finish phase one for me.

A Okay. At the same time that that was going on, the first weekend we were in there doing work, after this stuff was revealed to Sonny, I believe he came out on a Friday afternoon, and that's where Wanda and I's testimony differs a little bit. I remember that he came out on a Friday or I think it was a Friday and said he would have crews out after the Memorial Day weekend, as I recall it.

In the meantime I continued to try to get the garage apartment ready because, one, I was going to move my office in there and, two, we were going to utilize it to sleep in and try to get some of this other stuff in shape in a more reasonable manner.

So, we worked on this. I had my nephew over. He's on the ledgers that you had. That's Brett Smith. And we were readying the apartment to get it prepared. We [909] painted walls, we stripped floors, we sanded, we did all those sorts of things and I was reworking the windows—they had old windows in the house and I was reworking those. Some of the ropes had broken on them. And in the process of cleaning up, I discovered some areas of problems in the window in that garage apartment.

So by the time Sonny brought his crew out, there were more problems that had occurred. So, all of this stuff started going on and that was in phase one.

Q Okay. Now, that is all of phase one?

A No.

Q Okay. Go ahead with phase one.

A That—they started—Sonny came and viewed it, the upstairs portion of the garage apartment, underneath

the south wall by the windows there. He pulled the boards back because I discovered it with a vacuum cleaner in a window area. So he was there, pulled the boards back, looked at it for awhile, found a termite or some termites in it and said, yeah, this is another problem.

And I said, well, from what y'all have told me up to now, don't these guys come from the ground? Yeah. I said, well, doesn't it make sense that we go downstairs and see where this started from.

[910] So we went down on the south side of the garage and started pulling back—they had that side of the garage paneled, I don't know who paneled it, if it was the Gwins or people that owned it prior to them or whatever, but anyway, that garage had paneling in it. When they pulled the paneling back, they discovered significant damage to all the plating and the structures and whatnot in there.

Q Okay.

A So that was in phase one and it's probably all that was in phase one, I think.

Q Now we've covered phase one, right?

A I think.

Q Okay. Now, the conversation that you—that Tony Brown told you he heard John Buck say those statements that you identified for me, did that occur after phase one, during phase one or when did it occur?

A It would have had to have occurred after phase one.

Q Okay. Now, let's go to phase two.

There is a phase two, right?

A Well, I think there is, but there's a lot of phases and they really all kind of intermingled, but if I can—

* * * *

[918] Q Okay.

A —as I recall.

Q Now, phase two you've identified was the walls or basically—was it the rest of the walls in the garage area?

A It's every wall, every wall in the garage, the lower portion of the garage.

Q Okay.

A The lower level other than the south wall, which had previously been repaired.

Q Okay. Now, was that phase two or was there any other part of phase two that you remember?

A I believe that would probably suffice as what I referred to as phase two.

Q Okay.

A I think.

Q Okay. Now, let's go to—was there a phase three of repairs?

A Yeah.

Q Okay. Let's go to that then.

A Okay.

* * * *

[958] A That's correct, and then we started doing the—

Q And then you started moving in and then you started—you found some more damage over here which started phase two?

A As best I recall it as this point in time.

Q Do you remember any specific discussions other than what you've told me with Craig Jernigan or Sonny Adkison or any representative of Terminix concerning phase two work?

A Phase two work, as best I recall, I don't think Sonny came out personally to look at it. I made Jernigan aware of it. He notified them and I think that the person that came out and viewed it with Jernigan was John Buck. Now, I may be mistaken and I didn't have direct conversations with them.

I pointed out the work—I mean, the problems and they subsequently decided that it was their problem and gave Jernigan the go ahead to make whatever repairs were necessary.

Q Okay. That's what you remember on phase two discussions?

A As I recall, yes.

Q Okay. Now, we haven't yet identified phase [959] three, but let's do that now.

A I'm going to try to do that now and it may comingle with phase two somewhat, but I think—

Q Fine. Do the best you can.

A —the next thing that happened or it may have been in reverse or inverse order, but I don't think it is. I think phase three would be they peeled back the roof on the west side of the garage apartment, the shingle material and all that sort of thing.

Q Uh-huh.

A And that was done at my request because I had seen the extensive problems that had occurred to the roof area of the main house during phase one and I had also seen the problems on that south wall and I wasn't comfortable that we had found the problem. So—

Q Okay.

A To my recollection, that's what I call phase three. And phase three—

Q Was repairing the roof area on the garage?

A Phase three consisted of tearing off the west side of the roof of the garage, replacing every rafter, all the decking material and shingling it, yes.

Q And that was at Terminix' expense?

[960] A Yes.

Q Okay. Now, you've said a phase four?

A Uh-huh.

Q Now on phase three you understood the only work was to the garage area; is that right? There wasn't any on the main house?

A The best of my recollection, it was confined to the house—I mean, to the garage apartment.

Q What about discussions on the phase three work? You told me that you asked them and I assume when you say them—is that Craig Jernigan? Asked him to pull the roof back to see if there was damage?

A Craig Jernigan and his crew, yes.

Q And they pulled it back and there was damage?

A Yes.

Q And that was subsequently approved to be repaired by Terminix?

A That's correct.

Q Is that basically what you remember about conversations on phase three?

A Basically what I remember and Sonny, to my knowledge, did not even come out to talk about that. He relied on Jernigan's conversations.

[961] Q Okay. Phase four. Was there a phase four?

A Absolutely.

Q All right. What was phase four?

A Phase four was the problem that we were alluding to earlier along the—well—

Q Now, wait a minute. Phase two—and I'm sorry. I want to go back just a second before we go to phase four.

Phase two would have been starting around August of '91. Do you know when it finished up?

A They were able to do that work fairly rapidly and it was probably—that portion of it was probably completed in August.

Q Okay. So first of September phase two would have been completed?

A Right.

Q What about phase three; would it have started right after phase two?

A I'm having flashbacks right now and we're calling phase two and phase three are probably the same phase now as—

Q Okay.

A As I'm identifying my four phases again, those were all in and about the same period of time.

[962] Q So, those two could have been one and the same and all finished up in August?

A Probably so, as I recall, and, again, we can look at the records and figure out exactly when that was, but

as I reflect back on it, that was all nuked and done about —on or about the same time frame.

Q Okay. So now we're up to September of '91, right?

A Yeah, that was done in August because in August is when phase three started.

Q And finished up in August?

A I don't recall when phase three was finished up.

Q What about—

A Again, I've gone back and corrected what I told you before.

Q Right.

A This was all phase two, this garage apartment.

Q Phase two and three that you told me about really were combined into one phase?

A Was phase two.

* * * *

IN THE CIRCUIT COURT
FOR THE TWENTY-EIGHTH JUDICIAL CIRCUIT
OF ALABAMA
BALDWIN COUNTY

(Title Omitted in Printing)

The testimony of STEVEN CREW GWIN taken at the law offices of Messrs. Reams, Philips, Brooks, Schell, Gatson & Hudson, P.C., 3662 Dauphin Street, Mobile, Alabama on the 4th day of June, 1992, commencing at approximately 9:00 o'clock, a.m.

* * * *

[1340] Q Do you recall as your wife testified yesterday that you took possession of the house at 114 Fels Avenue in Fairhope somewhere around 1984?

A Right.

Q And then you made a decision to place it on the market for sale in 1991 and on February 9th of '91 entered into a sales authority with Irvine Realty?

A Yes.

Q Your wife told us, I believe, that there were four incidents between the time that you took possession in '84 and you put it on market in '91 wherein termites were seen, visably seen around the house.

Do you agree with that?

A Right.

Q Do you remember at the time that you listed the home for sale on February the 9th of 1991 that you had to complete something entitled a seller's disclosure statement?

A Yes.

* * * *

[1346] Q When the house was appraised, was there any mention made of termite damage at that time?

A I do not know if anyone made any mention of termite damage. I do not remember seeing the appraisal.

Q What conversations if any had you had with Terminex personnel, between September the 4th of '84 when you bought the house and May the 10th of '91 when you sold it, about termites?

A The only time I remember talking to Terminex was in '87 when I had found termites on the roof and found out that my bond had expired with Delta.

And, instead of trying to renew another bond with Delta, I decided to go with a national company like Terminex.

And I called Terminex and asked them to come out and see about setting the house, putting the house under bond. A gentleman came out—I don't remember who it was—and I met him at the house and told him where I had found the termites on the roof and pointed that area to him and showed him what I thought was termite damage on the side, on that northwest corner.

* * * *

IN THE CIRCUIT COURT
FOR THE TWENTY-EIGHTH JUDICIAL CIRCUIT
OF ALABAMA
BALDWIN COUNTY

(Title Omitted in Printing)

The testimony of GEORGE WALTER ADKISON taken at the law offices of Messrs. Reams, Philips, Brooks, Schell, Gaston & Hudson, P.C., 3662 Dauphin Street, Mobile, Alabama on the 4th day of June, 1992, commencing at approximately 1:00 o'clock, p.m.

* * * *

[1500] A There's just no way of knowing. We don't solicit them. They're called in to us and I have no way of telling how many will be called in.

Q During the last thirty days, what would you say you have done?

A I believe between twenty and thirty.

Q Is that a little busier than usual?

A There again, that's not something I can tell you. It's just according to the housing market at that time.

Q I'll leave you alone about that. Do you charge for giving these clearance letters?

A Yes, sir, we do.

Q What is the charge?

A Sixty dollars.

Q Do you only give them on property that you have under a termite protection plan?

A No, sir, we don't.

Q I don't understand that. Does that mean you will do it on any property?

A Yes, sir.

Q Is the charge any different if you have the property under a termite protection plan?

[1501] A At one time we didn't charge for clearance letters if they were under protection. But it is the same now.

Q When did that change take place?

A I'm not sure. It has been within the last six to eight months.

Q I asked you in the interrogatories if y'all had a termite bond on this property and the answer was no, on this 114 Fels Avenue.

A We have a termite protection on it.

Q Well, do you take—is it the word bond you take exception to?

A Yes, sir.

Q You don't call it a bond?

A No, sir.

Q Well, like Interrogatory Number 3: Please state whether you now have in force or have ever had in force a termite bond covering the subject property.

Answer: No.

If I had asked you if you had a termite protection plan covering the subject property, would your answer have been yes?

A Yes.

* * * *

IN THE CIRCUIT COURT FOR THE
TWENTY-EIGHTH JUDICIAL CIRCUIT OF
ALABAMA, BALDWIN COUNTY

(Title Omitted in Printing)

The testimony of JOHN WAYNE BUCK taken at the law offices of Messrs. Reams, Philips, Brooks, Schell, Gaston & Hudson, P.C., 3662 Dauphin Street, Mobile, Alabama on the 4th day of June, 1992, commencing at approximately 4:30 o'clock, p.m.

* * * *

[1613] JOHN WAYNE BUCK,

the witness, after having first been duly sworn to tell the truth, the whole truth, and nothing but the truth, was examined and testified as follows:

DIRECT EXAMINATION

BY MR. CHASON:

Q Tell us your name.
A John Wayne Buck.
Q Where are you from, John?
A Bay Minette.
Q How long have you been working at Terminex?
A Two years.
Q Do you live in Bay Minette now?
A Yes, sir.
Q Where do you live?
A End of Hand Avenue.
Q You went to work for them when?
A Sometime the end of May, '90.

Q Do you know the Dobsons?
A Yes. I know Mr. Dobson.
Q Are you familiar with their property in Fairhope?
A Uh-huh, sure.
[1614] Q When was the first time you ever went to that place?
A It was sometime early spring of '91. I don't recall the exact date.
Q What was the occasion for you going there?
A She had called in with some—well, not the Dobsons—but the Gwins had called in with some possible termite activity out there.
Q Did you talk to Mrs. Gwin?
A Well, I was there. I don't know if you call me the person in charge or not. I was there.
Q You got sent over there to check it out?
A Right.
Q Tell me what you found when you got there.
A I think Sonny was with me that time. I'm not sure. I think he was with me. I myself don't remember finding anything. That's just me. I don't know.
Q Was that when they reported the swarmer?
A Right, uh-huh.
Q Do you remember what you did when you got there?
A On that occasion seems like we checked the outside. I think I crawled underneath. If it wasn't that day, it was another day that I crawled underneath. [1615] I can't say for sure.
Q How many times did you go out there total?
A From what?
Q Ever have you been out there.
A Five or six maybe. Something like that.
Q Do you remember how many of them were when the Gwins were there and how many of them were after the Dobsons bought it?
A Maybe half and half. Something like that.

Q On this swarmer call in the spring of '91, how many times did you go in connection with that?

A A couple of times. Maybe two. Something like that.

Q You look like you don't remember too much about the details?

A I'm just—I go to so many places, I don't keep up, to tell you the truth.

Q Do you remember going underneath the house?

A Yes, sir.

Q Do you think it was in connection with the swarmer call, you think you went under the house?

A Yeah, uh-huh.

Q Did you find any termite damage under the house?

[1616] A Yes, sir, uh-huh.

Q Do you remember where you found it and what you found?

A Well, there's one thing sticks out in my mind is there's a sill—I guess it would be the east part of the house—that's really the only thing I can remember about the house itself.

Q What did you see over there?

A It was just a sill that had been one time or another riddled with termites. It just had termites in it.

Q I think we have got a picture of it here.

Look at these pictures marked 89-A, B and C and 88-A, B and C and let me ask you if that's the sill you're talking about?

A I don't have any idea.

Q Does that look like what it looked like, what you saw looked like?

A Something like that. I mean, I can't say that that is sill but, I mean, something like that.

Q Could be the sill you're talking about?

A I just—do you know what corner of the house this is in? I mean, do you have that?

[1617] Q I'm told—

MR. MOTES:

If you know, answer. If you don't, give your answer.

A No.

BY MR. CHASON:

Q Well, I'm told that is the sill on the east side of the house where the termites swarmed in March of '91.

I am asking you if you can tell me yes or no if that looks like it?

A No. To me, it doesn't.

Q It does not look like it?

A To me, it doesn't.

Q What is different about it?

A I just didn't remember it being white. That looks like white there. I just don't remember that.

Q But you did see a sill on that house that was riddled with termites?

A Yes, sir.

Q Did you see any active termites in it?

A No, sir.

Q Could you tell how long it had been since they

[1618] left?

A I can't.

Q Is there a way to tell whether it's been recently damaged by termites or whether it's old?

A Well, you can—I mean, well, let me see how to put this.

When they left, it's kind of like it dries up. And when they're in there it seems like it's a little moist.

When they leave, it just seems like it all just falls kind of to pieces or something.

Q Which way was this sill?

A It was dried up. I probed it, couldn't find anything in it.

Q That was in the area underneath the house where the termites had swarmed on the outside?

A Yes, sir. It's along that whole east side, though. She had mentioned something like that.

Q Did you think that the termites that she saw swarming on the outside were coming from the area of that sill that you saw on the underneath?

A Well, I had no way of knowing. All I could do was check the sill. That's just all I know.

[1619] Q How long was that sill that you are talking about?

A Well, as far as how much damage was—how far the damage was or . . .?.

Q Well, tell me both. How long was it and how much of it was damaged?

A Well, I guess the sill would run all the way down the east side but as far as the damage I don't remember it being—I don't know. Maybe ten feet either way, something like that. That's just a guess.

MR. MOTES:

Don't guess.

BY MR. CHASON:

Q Did you look around the rest of the house?
A Yes, sir.
Q Did you see any more damage?
A Not that I can recall.
Q That's the only damage you saw?
A That's what sticks out in my head. That's it.
Q Did you tell Sonny what you had found?
A Yes.
Q Did Sonny go under the house?

A At that time, I don't know. Now, he went [1620] another time with me but at that one instance I can't tell you whether he did or not.

Q Were y'all ever able to find any live termites anywhere around the place on that occasion?

A No, sir.

Q Did you take any boards loose?

A I didn't. I think they took a board off the window. I don't remember what was back there, to tell you the truth.

Q Did y'all put out any chemical that day?

A We treated it one day. I can't tell you if it was that day for sure.

Q Was that a one day deal or do you think that took more than one day to take care of this swarmer problem and treating it?

A I don't understand the question.

Q Did you have to come back more than one time to take care of the problems with the swarmers?

A Well, we came back and did more than one treatment. I mean, we treated one side of the house and then treated another side, on separate days.

Q Did you talk to Mrs. Gwin about what you had found?

[1621] A I spoke with her.

Q What did you tell her?

A I don't recall.

Q Did you have any way of knowing whether y'all had killed the termites, the colony that that swarm came from?

A With the treatment I did?

Q Yes.

A Well, when we treat it, we like to think that they are gone but, I mean, there's no hundred percent just proof that they are gone unless you just—I guess—just actually see into the wall there itself.

Q You don't ever know for sure?

A Very seldom.

Q Whenever termites swarm that means that they are present there somewhere, doesn't it?

A In the vicinity. It could be as far as, I'll say, maybe another yard or something. I mean, just because you have swarmers at one house doesn't mean that they would have to come from that property.

Q If Mrs. Gwin saw them swarming out from underneath a window, that wouldn't indicate that they came from that house?

[1622] A I didn't see it. I'd—if I had saw it myself, I could maybe say it. But I don't know. I have seen

them, well, go through windows maybe from the outside in. I have seen that.

Q Now, when was the next time you were out there after that?

A After the first time or—I was out there several times. I mean, do you. . .

Q I mean, I'm trying to get in order every time you went out there as best you can.

A All I know is that I went out there. I can't tell you an exact date or nothing.

Q Well, tell me however you remember, what it was for or. . .

A Well, I remember we went back out there and treated that over by the fireplace on the—it would be the Bay side of the house.

Q Was that at a later time?

A It would be, yes, I guess a later time.

Q What was the next time you went?

A I guess that would have to be for the letter itself.

Q What letter?

[1623] A The clearance letter itself.

Q Do you remember that you gave a clearance letter on this house?

A Well, I remember that the inspection we did was for a clearance letter.

Q When is the last time you have seen that clearance letter?

A I couldn't tell you.

Q Have you seen it since you gave it?

A Yes, we've seen it.

Q When have you seen it?

A I saw it over at Mr. Motes' office.

Q When is that?

A A couple of weeks ago.

Q What about before that? When is the last time you saw it?

A I guess when we gave it.

Q You hadn't looked at it since you gave the letter the until you saw it a couple of weeks ago?

A Not as I can recall.

Q What do you remember about the request for that clearance letter?

A I really don't remember anything about the [1624] request. I wasn't in on the ordering of it or anything. I was there just to do it.

Q Did you do the inspection?

A Yes, sir.

Q What did you do?

A Well, just what we do on an inspection. We just check the property, go under it, probe areas.

Q Did you do that?

A Yes, sir.

Q Went all underneath the house?

A Yes, sir.

Q Did you go in the attic?

A Not at that time.

Q What time did you go in the attic?

A Mrs. Gwin took us through the house and all through the house and the garage—I guess you call it a garage apartment.

Q When was that?

A I don't—it was just sometime prior to that.

Q What else did you do on your inspection?

A Well, you just—just what we do on inspections, just check and probe and just do a visual inspection on it.

[1625] Q Did you see anything different under the house on May the 7th than you had on your first time, which I think we have agreed is March 28th?

A Not that I can recall.

Q Did you see any live termites?

A No, sir.

Q Did you talk to Mrs. Gwin about what you saw?

A I don't recall.

Q Was anybody with you when you did that inspection?

A It seems like Sonny was but. . .

Q Did he go under the house?

A Yes, sir.

Q So y'all both went under the house?

A Yes, sir.

Q Was there any reason you all both went under the house?

A Well, that's just something we do sometimes. It just makes things a little easier.

Q You split it up, he looked at half and you looked at half?

A Well, you just kind of—not necessarily that. You just—seems like two heads are better than one [1626] sometimes.

Q Were y'all particularly cautious or careful about this particular inspection since they had a good bit of trouble out there?

A I like to think we were.

Q Why don't you tell me in your own words why you were being particularly careful of this inspection?

A Well, she had had a call of possible swarmers.

Q Had you looked at her file or the file on that property?

A No, sir.

Q Were you aware that that was not the first time she had reported swarmers?

A No, sir.

Q You didn't know that?

A No, sir.

Q You had seen some damage under the house, though?

A Yes.

Q The fact that she she had reported swarmers and the fact that she had termite damage under her house, did that cause you to believe maybe there was a pretty

high chance that she had an active infestation of [1627] termites there?

A Just didn't know. I mean, I just didn't know.

Q Did you fill out the letter you see there in front of you?

A This right here?

MR. MOTES:

Terminex 2.

BY MR. CHASON:

Q Yes.

A No, sir. I think I just signed it.

Q Who filled it out?

A Well, the secretaries do the actual typing of the letters.

Q Did you draw the graph on the second page?

A Yes, sir. That's my handwriting there.

Q Is that graph accurate?

A It should be.

Q You found damage in all the spots that are shown there?

A Yes, sir.

Q Now, what was the next time you went out there?

A It's just hard to say. Maybe when the Dobsons got it. I just don't know.

[1628] Q What would be the reason for you going out there?

A If they had damage or maybe some more termites or something.

Q You don't remember particularly when or why?

A No, sir, I sure don't.

Q You get paid what, a salary and then a commission on top of that?

A Yes, sir.

Q How do they figure your commission?

A You just make units on what you do. I mean, you just have to make your—you have to make your salary. Then you make commission above your salary. So it's just you have to make everything you get.

Q How do you make it?

A Well, just whatever job you do you just get paid in a certain way for it. Everything has different—we get paid on units. Everything you do you get different units for.

* * * *

IN THE CIRCUIT COURT
OF BALDWIN COUNTY, ALABAMA

Case No. CV-91-796

G. MICHAEL DOBSON and WANDA C. DOBSON,
Plaintiffs,

vs.

THE TERMINIX INTERNATIONAL COMPANY, L.P., ALLIED-BRUCE TERMINIX COMPANIES, INC., d/b/a Terminix Service, STEVEN C. GWIN and JAN A. GWIN,
Defendants.

FIRST AMENDED COMPLAINT

[Filed Jun. 25, 1992]

Come now the Plaintiffs in the above styled cause on this their First Amended Complaint and in the place and stead of the Defendant referred to in the original Complaint as "Terminix Service" do substitute therefore as a party Defendant Allied-Bruce Terminix Companies, Inc., d/b/a Terminix Service.

Plaintiffs do further amend the Complaint on file in this cause to include the following:

COUNT ONE

Count One of the Complaint is amended by adding thereto the following:

8. That the Defendant, Allied-Bruce Terminix Companies, Inc., d/b/a Terminix Services, at the time and place complained of herein was acting within the line and scope of its authority either as the agent, servant, employee or alter ego of the Defendant, Terminix International Company, L.P., such that both the said Defend-

ant, Allied-Bruce Terminix Companies, Inc., d/b/a Terminix Service, and the Defendant, Terminix International Company, L.P., are liable for the said misrepresentations to the Plaintiffs referred to herein.

WHEREFORE, Plaintiffs demand judgment against the Defendants for such damages to which they might be entitled, in excess of the jurisdiction of this court, and including punitive damages, together with interest and costs.

COUNT TWO

By adding the following to Count Two:

WHEREFORE, Plaintiffs demand judgment against the Defendants for such damages to which they might be entitled in excess of the jurisdiction of this court, and including punitive damages, together with interest and costs.

COUNT THREE

By adding the following to Count Three:

WHEREFORE, Plaintiffs demand judgment against the Defendants for such damages to which they might be entitled, in excess of the jurisdiction of this court, and including punitive damages, together with interest and costs.

COUNT FOUR

Come now the Plaintiffs in the above styled cause and claim damages of the Defendants, The Terminix International Company, L.P. and Allied-Bruce Terminix Companies, Inc., and as grounds therefor would show unto the Court as follows:

1. Plaintiffs herein reallege the allegations of Paragraph One of Count One of the Complaint.

2. That at all times since August 25, 1987, the Defendants, Gwin, had in force a Termite Protection Plan issued by the Defendant, Terminix, and bearing guarantee number PR08870291-08 covering the premises located at 114 Fels Avenue, Fairhope, Alabama.

3. That under and by the terms of the contract of sale of said premises from Gwin to the Plaintiffs, the Plaintiffs were to cause said Termite Protection Plan to be transferred to the Plaintiffs along with "written evidence from a bonded and licensed termite control company that a visual inspection by them indicates the dwelling is free from infestation by wood destroying insects and damage caused by currently active infestation."

4. That on May 10, 1991, said Termite Protection Plan was transferred to the Plaintiffs and which plan the Plaintiffs have maintained in force through the present date by paying all fees and charges due thereunder.

5. That under and by the terms of said Termite Protection Plan, the said Defendants, Terminix, agreed to provide the necessary service "to protect the identified property against the attack of subterranean termites" and upon the breach thereof to "arrange for the necessary repairs" and to pay for the same.

6. That the Defendants, Terminix, have breached the terms of said Termite Protection Plan by failing to protect the identified property against the attack of subterranean termites, in that said dwelling has, since the purchase by the Plaintiffs, been infested throughout with live termites; and in that said Defendants, Terminix, did not arrange for all of the repairs rendered necessary by or pay for the same, but rather that the Plaintiffs were required to arrange for and pay for many of said repairs.

7. That as a proximate result of said breach, the Plaintiffs have suffered damages in that they have been required to retain substitute housing while repairs have been made to the dwelling which they purchased; that portions of their dwelling remain damaged from infestation; that they have been caused to suffer mental anguish;

and that their dwelling has been rendered less valuable because of the fear of future termite infestations.

WHEREFORE, Plaintiffs demand judgment against the Defendants for such damage to which they might be entitled, in excess of the jurisdiction of this court, together with interest and costs.

/s/ Allan R. Chason
ALLAN R. CHASON
Attorney for Plaintiffs

Of Counsel:
CHASON & CHASON, P.C.
P.O. Box 100
Bay Minette, Alabama 36507

Plaintiffs respectfully request a trial by jury of all issues stated in the foregoing First Amended Complaint.

/s/ Allan R. Chason
ALLAN R. CHASON
Attorney for Plaintiffs

(Certificate of Service Omitted in Printing)

IN THE CIRCUIT COURT
OF BALDWIN COUNTY, ALABAMA

(Title Omitted in Printing)

CROSSCLAIM

[Filed Jun. 30, 1992]

COMES NOW Steven C. and Jan A. Gwin, two of the defendants in this cause, and file this their crossclaim against the Terminex International Company LP and Allied Bruce Terminex Companies, Inc. d/b/a Terminex Service as follows:

COUNT ONE

1. On or about August 25, 1987, the crossclaim plaintiffs, Steven C. and Jan A. Gwin, entered into a contract known as a "Termite Protection Plan", Guarantee No. PR08870291-08 with the crossclaim defendants whereby the crossclaim defendants for a consideration paid by the crossclaim plaintiffs agreed to provide the necessary service to protect the crossclaim plaintiffs' dwelling against the attack of subterranean termites. A copy of the Termite Protection Plan, Guarantee No. PR08870291-08 is attached hereto and marked as Exhibit A. This contract was extended on its anniversary date for the years 1988, 1989, and 1990.

2. Based on information discovered in this case, the counterclaim defendants breached its Termite Protection Plan and extensions thereof in that subterranean termites were apparently allowed to cause damage to the structure and walls of the counterclaim plaintiffs' dwelling.

3. As a proximate result of said breach of contract, the counterclaim plaintiffs have been caused to suffer the following damages:

a. Their home was permanently damaged and made less valuable;

b. Repairs that should have been made by the plaintiffs' crossclaim defendants pursuant to the Termite Protection Plan were not made, and demand has been made on the crossclaim to effectuate and pay for said repairs;

c. They have been required to expend monies to defend a lawsuit filed by the purchasers of their home, G. Michael Dobson and Wanda C. Dobson, the plaintiffs in this lawsuit arising out of the home's infestation of subterranean termites;

d. They have suffered and continue to suffer mental pain and anguish.

WHEREFORE, crossclaim plaintiffs demand judgment against the crossclaim defendants for whatever amount the crossclaim plaintiffs may be liable to the plaintiffs, if any, and in addition such damages as the trier of fact may assess.

COUNT TWO

4. Crossclaim plaintiffs incorporate by reference paragraph 1.

5. Between August 25, 1987 and May 10, 1991, the crossclaim defendants were negligent in the manner in which they inspected the crossclaim plaintiffs' home, in the way they treated the crossclaim plaintiffs' home for subterranean termites, and in the manner in which they performed the general conditions of their Termite Protection Plan, Guarantee No. PR08870291-08.

6. As a proximate cause of said negligence, the counterclaim plaintiffs have been caused to suffer the following damages:

a. Their home was permanently damaged and made less valuable;

b. Repairs that should have been made by the crossclaim defendants pursuant to the Termite Protection Plan were not made, and demand has been made on the plaintiffs' crossclaim to effectuate and pay for said repairs;

c. They have been required to expend monies to defend a lawsuit filed by the purchasers of their home, G. Michael Dobson and Wanda C. Dobson, the plaintiffs in this lawsuit arising out of the home's infestation of subterranean termites;

d. They have suffered and continue to suffer mental pain and anguish.

WHEREFORE, crossclaim plaintiffs demand judgment against the crossclaim defendants for whatever amount the crossclaim plaintiffs may be liable to the plaintiffs, if any, and in addition such damages as the trier of fact may assess.

/s/ Mark A. Newell
MARK A. NEWELL
Attorney for Defendants
Steven C. Gwin and
Jan A. Gwin

Of Counsel:
BARKER & JANECKY, P.C.
3300 First National Bank Building
Post Office Box 2987
Mobile, Alabama 36652
(205) 432-8786

(Certificate of Service Omitted in Printing)

KEY #33073 R200 87

CONTRACT CURRENT THRU 8/91.

TERMINIX. INTERNATIONAL

THE TERMINIX INTERNATIONAL COMPANY L.P.

TERMITE PROTECTION PLAN

GUARANTEE NO. PR 08870291-08

C
011-02
632F

TRANSFERRED TO: G Michael Dobson

PURCHASER Steve G#in TELEPHONE _____

MAIL ADDRESS 114 Fels

CITY Fairhope, STATE Al ZIP CODE 36532

DESCRIPTION OF PROPERTY Residence

PROPERTY ADDRESS _____

CITY _____ STATE _____ ZIP CODE _____

Effective 8/25/87 through 8/14/88, for the sum of $ 585.87 Terminix will provide the necessary service to protect the identified property against the attack of subterranean termites *(Reticulitermes sp., Heterotermes sp.)*.

Terminix will extend protection annually to the original owner for the LIFETIME of the identified property subject to the general conditions of this agreement for $ 65.87 per year payable on or before the end of the previous protection period. After the third year and each year thereafter, Terminix reserves the right to revise the annual extension charge. After this Plan is renewed beyond the initial contract term, Terminix will periodically reinspect the identified property and any further treatment found necessary will be performed free.

In the event of additions or alterations to the identified property, Purchaser must arrange with Terminix for additional service which may require an adjustment to the annual extension charge.

This Plan provides protection against new subterranean termite damage to the structure and contents. If new damage occurs during the contract term, Terminix will, upon notification and inspection, arrange for the necessary repairs and pay the cost of labor and materials not to exceed $100,000. New damage is damage associated with an active termite infestation. Unless live termites are found in the damaged area, the damage discovered is old damage and not covered under this Plan.

Upon transfer of ownership of the identified property, protection against subterranean termites may be continued upon the request of the new owner and upon payment of a contract transfer fee of $ 25.00. In addition, Terminix reserves the right to revise the annual extension charge upon transfer of ownership. In the event the new owner fails to request continued coverage or does not agree to pay the transfer fee or the revised annual extension charge, the Termite Protection Plan will terminate automatically as of the date of this change of ownership.

Any additional provisions attached hereto including the general conditions and arbitration provision on the reverse side and the inspection graph dated 8/25/87 are part of this plan.

THE TERMINIX INTERNATIONAL COMPANY L.P. hereby guarantees the fulfillment of the terms of this Plan.

EXHIBIT A

Carlos H Carter

BY _____
TERMINIX MANAGER

EXECUTED AT MEMPHIS, TENNESSEE

59

201

110799

D.P. – A/R ACCT. NO.

DIV.	RT. #	ZONE	ACCT. NO.
08			104200

☒ NEW D.P. ACCT. NO.
☐ EXISTING D.P. ACCT. NO.

INVOICE

Terminix Service

P.O. BOX 1830
DAPHNE, AL 36526

TERMINIX
TERMITE and PEST CON

8/26/87
DATE

Steve Gwin
114 Fels Ave
Fairhope, Al 36532

$_____
AMOUNT PAID

Please detach and return with check - thank you.

	Effective Date	Circle One	Rate
☐ Pest Service Contract $_____	_____	E1 – E2 – M – Q1 – Q2 – Q3	$_____
☒ Termite Protection $ 585.87	☐ New Bldg. ☒ Existing Bldg.		_____ Phone
☐ Special Work $_____	Type_____		

Service Address_____

Lot _____ Sub-Division _____

*TERMS OR SPECIAL INSTRUCTIONS:
102 ev 532F

INVOICE AMOUNT $_____
TAX (If Applicable) $_____
INVOICE TOTAL $ 585.87
Paid On Completion $ -0-
* NOW DUE $ 585.87

CUSTOMER COPY

Thank You!

110799

IN THE CIRCUIT COURT FOR THE
TWENTY-EIGHTH JUDICIAL CIRCUIT OF
ALABAMA, BALDWIN COUNTY

Civil Action Number CV-91-796

G. MICHAEL DOBSON and WANDA C. DOBSON,
Plaintiffs,

VS.

THE TERMINIX INTERNATIONAL COMPANY, L.P.,
TERMINIX SERVICE, STEVEN C. GWIN and JAN A. GWIN,
Defendants.

Civil Action Number CV-92-197

STATE FARM FIRE & CASUALTY COMPANY,
Plaintiff,

VS.

STEVEN C. GWIN, JAN A. GWIN, G. MICHAEL DOBSON
and WANDA C. DOBSON,
Defendants.

The testimony of WILLIAM DANIEL CALHOUN, taken at the Law Offices of Irby & Heard, 317 Magnolia Avenue, Fairhope, Alabama, on the 20th day of July, 1992, commencing at approximately 3:00 o'clock, p.m.

* * * *

[1652] Q Okay. Then the commission for Irvine Company would be included on the second page at the very top right?

A That's correct.

Q I think five thousand four hundred, and fifty cents?

A Right.

Q I got it right that time. What about if there's any charge for the wood infestation report or the transfer of the termite protection plan, would there be any—where would that be noted?

A Here, where it says pest inspection.

Q Would both charges be shown down there if there were any?

A Generally, yeah, they are. You know, if there's a charge for a clearance letter, that charge would be shown. I—generally I don't think Terminix charges a—makes any charges for the transfer of a termite bond.

Q Was Terminix paid anything, based on that closing statement, for the wood infestation report presented to you at closing?

A Apparently not, according to this closing statement.

Q Let me show you what's marked Defendant's Exhibit [1653] 4, 5, and then I think 6 is just a copy, again, of the first page of 5 with additional signatures at the bottom, and ask you if you remember these documents being present at closing, also?

A Yes, they were.

Q All—both—all three?

A All three, yes.

Q And was Number 2 two pages as it is there with a graph attached? That is Number 5, I mean.

A Yes. That would be correct.

Q Okay. Now, can you tell me what you remember about discussing at the closing, if anything, about termite problem, termite damage, or termite infestation?

A Generally what I do—and I'm sure it's probably—it is the way I handled this closing. You know, primarily you look to see if there is any active infestation or any evidence of any active infestation of wood-destroying insects. And which this states no visible evidence of infestation of wood-destroying insects. I think there was some discussion of the—I know there was some discussion of the previous damage that is shown here on the graph.

Q Do you remember what that discussion was?

A As far as I recall, I generally state that it is [1654] not—it is not uncommon for—an older house, and it was my understanding that this was an older house, I hadn't viewed the house, I knew the general location of it, that it is not unusual for there to be some previous damage in a—in a house of—you know, that may be thirty, forty or so years old.

And that's fairly—fairly common. The contract calls that there be—that the termite report state that there be no evidence of active infestation of wood-destroying insects, which this one does state.

Q Okay. Now, were all three of these documents, to your knowledge, presented to the purchaser, the Dobsons, at the closing?

A Yes. I'm sure they—they were discussed with the Dobsons at closing.

Q And, in fact, I think six shows signatures?

A Right. Exactly. And also the termite—it was explained to them that there was an existing termite bond on the property that was being transferred.

Q What, if anything, would be said about the coverage provided by the termite protection plan?

A I generally don't get into the discussion of that.

* * * *

205-928-9248
P. O. Box 1436, Fairhope, AL 36533

Irvine co. inc. Real Estate

FOR IDENTIFICATION (1)
DTD 205-990-7170
27986 Highway 98, Daphne, AL 36527

1664

PURCHASE AGREEMENT

Date 29 March 19 91 6:00 AM/PM

1. THE UNDERSIGNED, HEREINAFTER CALLED THE BUYER, HEREBY OFFERS TO BUY THE PROPERTY located in the city of Fairhope County of Baldwin, Alabama, commonly known as 114 Fels and legally described as: Lot 3 + West 2 ft. of Lot 2 Block 14, according to Plat No. 6 p. 38 for the sum of (exactly) Seventy-Seven Thousand One Hundred and Fifty Dollars ($ 77,150).

2. THE TERMS OF PURCHASE SHALL BE as indicated by "x" below: (other unmarked terms of purchase do not apply).

CASH: ( ) The full purchase price upon execution and delivery of Warranty Deed/Bill of Sale.

NEW MTG: (X) The full purchase price upon execution and delivery of Warranty Deed/Bill of Sale, contingent upon Buyer's ability to obtain a 30 year FHA (type) mortgage, in the amount of $ 77500 bearing an interest rate not to exceed 9½ % computed monthly, on or before the date the sale is to be closed, which Buyer agrees to apply for immediately and accept promptly if tendered. The appraisal fee and cost of credit report, if any, shall be paid at time of application by Buyer. Buyer is to pay the loan closing cost including prepaid items, closing fees (except those not allowed on VA loan) and recording fee. Discount points, not to exceed 1 to be paid by (Buyer/~~Seller~~). Origination fee not to exceed 1 points shall be paid by (Buyer/Seller). Seller agrees to pay deed preparation fee. On FHA mortgages it is expressly agreed that, notwithstanding any other provisions of this contract, the Buyer shall not be obligated to complete the purchase of the property described herein or to incur any penalty by forfeiture of earnest money deposits or otherwise unless the Seller has delivered to the Buyer a written statement issued by the Federal Housing Commissioner or a Direct Endorsement Lender setting forth the appraised value of the property (excluding closing costs) of not less than $ 77150.00 which statement the Seller hereby agrees to deliver to the Buyer promptly after such appraised value statement is made available to Seller. The Buyer shall, however, have the privilege and option of proceeding with the consummation of the contract without regard to the amount of the appraised valuation. The appraised valuation is arrived at to determine the maximum mortgage the Department of Housing and Urban Development will insure. HUD does not warrant the value or the condition of the property. The Purchaser should satisfy himself/herself that the price and condition of the property are acceptable. (Buyer/Seller) agrees to meet any repair or other requirements for mortgage loan purposes, not to exceed $_____.

VENDOR'S LIEN: ( ) $_____ upon execution and delivery of Warranty Deed/Bill of Sale with Vendor's Lien reserved wherein the balance of $_____ shall be payable in (_____monthly _____annual) installments of $_____ (including/plus) interest at _____% per annum. Interest to start on date of closing and the first payment to become due _____ after closing. No penalty for prepayment. Buyer to pay closing fee and recording fee. Vendor's Lien (shall/shall not) be assumable without written consent of lien holder, and the Vendor's Lien or Note (shall/shall not) contain a late charge provision of _____% of an installment when paid more than _____ days after due date thereof. Buyer to supply a one year hazard insurance policy at closing with standard mortgage clause. Buyer agrees to provide, at his/her expense, a credit report, verification of income and other financial data satisfactory to Seller.

EQUITY: ( ) Upon execution and delivery of Warranty Deed/Bill of Sale assuming existing mortgage or Vendor's Lien, Buyer to pay the difference (approx./exactly) $_____ between the purchase price above and the unpaid balance (approx./exactly) $_____ of said mortgage or Vendor's Lien which Buyer agrees to assume and pay at an interest rate not to exceed _____%. Seller agrees to transfer tax escrow amounts to Buyer in proper balance and interest is to be prorated to date of closing. In the event the existing insurance policy is assumed by the Buyer, the premium will be prorated as of the date of closing. Mortgage payment to be current at time of closing. Buyer to pay mortgage transfer fee, recording fee and all other costs and fees charged by lender. Seller (shall/shall not) be released of liability for the indebtedness being assumed. If mortgagee approval is required for assumption, this contract is contingent upon such approval and Buyers agree to apply for mortgage assumption immediately.

3. AGENCY DISCLOSURE: The listing agency Irvine Co Inc. represents the Seller (unless otherwise stated), and the selling agency IRVINE Co. Inc. represents the (X) Seller ( ) Buyer. Seller's initials _____ Buyer's initials JHW.

4. OTHER PROVISIONS: Subject to approval of Fairhope Single Tax Corporation. Subject to marketable title as defined in paragraph 9 of this contract.

5. ALL IMPROVEMENTS, PERMANENT FIXTURES, AND APPURTENANCES ARE INCLUDED in the purchase price, except Mirror in bathroom and do include curtain fixtures in bedroom + kitchen.

6. A HOME OWNER'S WARRANTY (will/~~will not~~) be provided at closing by (Buyer/Seller).

7. SALE SHALL BE CLOSED and deed delivered on or before 30 April 19 91. Time shall be of the essence with all terms, conditions and particulars of this agreement. Title to be taken in the names of G. Michael + Wanda C. Dobson (with/without) right of survivorship in a form satisfactory to Buyers. The property is sold and is to be conveyed subject to any mineral and mining rights not owned by Seller and subject to present zoning and flood plain classification, utility easements, covenants and restrictions and building set back line. Seller owned mineral rights do _____ do not X transfer.

8. POSSESSION OF THE PROPERTY is to be given the Buyer on or before = JHW days after closing. In the event possession cannot be given on such date, Seller shall pay $ — per day as rental after such period, but will vacate by — without fail.

9. AN OWNER'S POLICY of title insurance in the amount of the purchase price is to be furnished by the Seller. Mortgagee title insurance and closing fee shall be paid for by the Buyer. A current survey shall be provided prior to closing and will be paid for by the (Buyer/Seller).

10. FOR VALUABLE CONSIDERATION, Buyer gives the Listing Broker, named above until 5:00 PM AM/PM to obtain the written acceptance of this offer and agrees that this offer, when signed, will constitute a binding agreement between Buyer and Seller and herewith deposits $ 1000.00 (check/cash) evidencing Buyer's good faith. Said funds are to be deposited in escrow by said Selling Broker and shall be applied to the purchase price on the date of closing. If this offer is not accepted or the title is not marketable, or if the terms of purchase are contingent upon ability to obtain new mortgage or Vendor's Lien or other contingencies as specified which cannot be met, this deposit shall be refunded. In the event of default by Buyer, all deposits made hereunder may be forfeited as liquidated damages at Seller's election, or alternatively, Seller may retain such deposits as part payment of the purchase price and pursue his legal and equitable remedies hereunder against Buyer. A mutual release signed by all parties to this contract will be required before any funds can be released. Earnest money to be applied upon acceptance of offer.

11. BUYERS AND SELLERS acknowledge that they have read paragraphs 16 through 23 on the reverse of this page and that these paragraphs are part of this contract. Buyers and Sellers acknowledge receipt of a copy of this agreement. Seller's initials _____ Buyer's initials JHW

Witness Frankie Evans — x [signature] — Buyer SS# 436-52-3921
Buyer's Address P.O. Box 557 — x [signature] — Buyer SS# 434-76-1475
Bay Clear AL 36564 — Phones: Res. 928 3745 — Office 342 4250

SELLER'S ACCEPTANCE: Dated: _____ 19____ _____ AM/PM

12. THE ABOVE OFFER IS HEREBY ACCEPTED _____

13. IN THE EVENT A COUNTER OFFER is made, it shall expire on _____ _____ AM/PM if Buyer has not given prior written acceptance.

14. SELLER AGREES TO PAY LISTING BROKER a commission in accordance with the signed Sales Authority for negotiating this sale. If Buyer defaults, the earnest money shall be split between the Seller and Listing Broker in accordance with the Sales Authority.

Witness [illegible] — x [signature] — Seller SS# 412-21-1157
Seller's Address 114 Fels Ave — [signature] — Seller SS# 416 78 6916
Fairhope AL 36532 — Phones: Res. 928 4918 — Office 1132 1725

BUYER'S ACCEPTANCE OF COUNTER OFFER/RECEIPT OF ACCEPTANCE:

15. BUYER ACKNOWLEDGES RECEIPT of Seller's acceptance of Buyer's offer. In the event this acceptance was subject to certain changes from the Buyer's offer, the Buyer agrees to accept said changes. All other provisions of the original [illegible]

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16. SELLER IS TO FURNISH WRITTEN EVIDENCE from a bonded and licensed termite control company that a visual inspection by them indicates the dwelling is free from infestation by wood destroying insects and damage caused by currently active infestation. OLD DAMAGE IS NOT CONSIDERED. The current termite contract, if any, is to be transferred to Buyer at Buyer's expense.

17. ALL PROPERTY TAXES, except of equity sales with escrow account, and any rentals being collected from existing tenants, to be prorated at time of closing.

18. PROPERTY ASSESSMENTS which become a lien on the property prior to closing date shall be paid by the Seller, without proration. Any special improvements now installed, but not yet a lien, shall be assumed by the Buyer.

19. THE PURCHASE PRICE AND TERMS OF THIS SALE MAY BE DISCLOSED by the REAL ESTATE CO. in the ordinary conduct of their business.

20. THE FOREGOING CONSTITUTES THE entire agreement. No terms or conditions agreed on verbally will be recognized. Any change must be in writing and approved by all parties. Real Estate agents are not to be held liable for any conditions or non-performance of this agreement.

21. NEITHER SELLER NOR ANY AGENT MAKES ANY REPRESENTATIONS OR WARRANTIES, EITHER VERBAL OR IMPLIED, REGARDING THE CONDITION OF THE PROPERTY EXCEPT TO THE EXTENT EXPRESSLY AND SPECIFICALLY SET FORTH HEREIN. Buyer has the obligation to determine, either personally or through or with a representative of Buyer's choosing, any and all conditions of the property without limitation, the condition of the heating, cooling, plumbing and electrical systems and any built-in appliances and the roof and the basement, including leaks therein; the size and area of the property, construction materials, including floors, structural condition; utility sewer or septic tank availability and condition/subsurface conditions, potentially hazardous gases, including radon, and any matters affecting the character of the neighborhood. BUYER HAS EXAMINED THIS PROPERTY AND AGREES TO ACCEPT SAME IN ITS PRESENT CONDITION, EXCEPT AS MAY BE SPECIFIED HEREIN.

22. HEATING, COOLING, PLUMBING AND ELECTRICAL systems and all included appliances shall be warranted by Seller to be in working order at time of conveyance. Buyer or his representative shall be responsible for inspection of same prior to conveyance. Inspection expense, if any, shall be paid by the Buyer.

23. A FURTHER PERIOD OF 30 days shall be allowed for closing if (a) the closing is delayed by reason of delays in abstracting or by title defects which can be readily corrected, or if (b) the terms of the purchase require a new mortgage and the lender issues a commitment prior to the date of closing, but is delayed in consummating the mortgage. Risk or loss by fire or other casualty, or condemnation shall be on the Seller until title is conveyed.

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AMENDATORY CLAUSE

"It is expressly agreed that notwithstanding any other provisions of this contract, the purchaser shall not be obligated to complete the purchase of the property described herein or to incur any penalty by forfeiture of earnest money deposits or otherwise unless the mortgagee has delivered to the purchaser a written statement issued by the Federal Housing Commissioner or a Direct Endorsement lender setting forth the appraised value of the property (excluding closing costs) of not less than $ 77,150.00 which statement the mortgagee hereby agrees to deliver to the purchaser promptly after such appraised value statement is made available to the mortgagee. The purchaser shall, however, have the privilege and option of proceeding with consummation of the contract without regard to the amount of the appraised valuation. The appraised valuation is arrived at to determine the maximum mortgage the Department of Housing and Urban Development will insure. HUD does not warrant the value nor the condition of the property. The purchaser should satisfy himself/herself that the price and condition of the property are acceptable."

Signed:

Borrower
G. MICHAEL DOBSON

Borrower
WANDA C. DOBSON

Seller
STEVEN C. GWIN

Seller
JAN A. GWIN

FRM 9002
Rev. 7/90

67

205-928-9248
P. O. BOX 1436, FAIRHOPE, AL 36533

Irvine
co. inc.
Real Estate

205-626-7170
27985 HIGHWAY 98, DAPHNE, AL 36526

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ADDENDUM

1. This is an amendment to the PURCHASE AGREEMENT covering the _____ real property, ___X___ leasehold property commonly known as 114 Fels Ave - Fairhope, Al dated 29 March 1991 between G. Michael + Wanda C. Dobson (Buyer) and Steven C. + Jan A. Erwin (Seller).

2. Applicable conditions of the purchase shall be as indicated by an "X" below and initialed by the buyer. (Other unmarked conditions do not apply.)

a. _____ For an equity sale, assuming the existing mortgage:

(1) Copy of said mortgage is attached and acknowledged to have been received by buyer. _____ / _____ (Buyers' initials)

(2) Offer is made subject to receiving copy of said mortgage. _____ / _____ (Buyers' initials)

b. _____ If subject to any existing recorded restrictions, easements, reservation or leases:

(1) Copy is attached and acknowledge to have been received by buyers. _____ / _____ (Buyers initials).

(2) Offer is made subject to receiving applicable copies. _____ / _____. (Buyers' initials)

3. THE UNDERSIGNED PARTIES HEREBY AGREE TO ANY ADDITIONAL TERMS OR CONDITIONS AS FOLLOWS:

The closing date of April 30, 1991 has been extended until on or before May 15, 1991.

4. The terms of this addendum, upon its execution by both parties, are herewith made an integral part of the aforementioned Purchase Agreement.

Date: 4/24/91 Time: 1:40 P.M.

G. Michael Dobson (Buyer)

Wanda C. Dobson (Buyer)

Date: 4/25/91 Time: 5:05 PM

x _____ (Seller)

x Jan A Erwin (Seller)

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CONTRACT CURRENT THRU 8/91.

KEY #33073 REV. 4/87

TERMINIX INTERNATIONAL

THE TERMINIX INTERNATIONAL COMPANY L.P.

TERMITE PROTECTION PLAN

GUARANTEE NO. PR 08870291-08

C
011-02
632F

TRANSFERRED TO: G Michael Dobson

PURCHASER Steve Gwin TELEPHONE

MAIL ADDRESS 114 Fels

CITY Fairhope, STATE Al ZIP CODE 36532

DESCRIPTION OF PROPERTY Residence

PROPERTY ADDRESS

CITY STATE ZIP CODE

Effective 8/25/87 through 8/14/88, for the sum of $ 585.87 Terminix will provide the necessary service to protect the identified property against the attack of subterranean termites *(Reticulitermes sp., Heterotermes sp.)*.

Terminix will extend protection annually to the original owner for the LIFETIME of the identified property subject to the general conditions of this agreement for $ 65.87 per year payable on or before the end of the previous protection period. After the third year and each year thereafter, Terminix reserves the [illegible] annual extension charge. After this Plan is renewed beyond the initial contract term, Terminix will periodically reinspect the identified property and any further treatment found necessary will be performed free.

In the event of additions or alterations to the identified property, Purchaser must arrange with Terminix for additional service which may require an adjustment to the annual extension charge.

This Plan provides protection against new subterranean termite damage to the structure and contents. If new damage occurs during the contract term, Terminix will, upon notification and inspection, arrange for the necessary repairs and pay the cost of labor and materials not to exceed $100,000. New damage is damage associated with an active termite infestation. Unless live termites are found in the damaged area, the damage discovered is old damage and not covered under this Plan.

Upon transfer of ownership of the identified property, protection against subterranean termites may be continued upon the request of the new owner and upon payment of a contract transfer fee of $ 25.00. In addition, Terminix reserves the right to revise the annual extension charge upon transfer of ownership. In the event the new owner fails to request continued coverage or does not agree to pay the transfer fee or the revised annual extension charge, the Termite Protection Plan will terminate automatically as of the date of this change of ownership.

Any additional provisions attached hereto including the general conditions and arbitration provision on the reverse side and the inspection graph dated 8/25/87 are part of this plan.

FOR IDENTIFICATION
D EX
11-19-92 AJC

THE TERMINIX INTERNATIONAL COMPANY L.P. hereby guarantees the fulfillment of the terms of this Plan.

Carlon H Carter

BY
TERMINIX MANAGER

EXECUTED AT MEMPHIS, TENNESSEE

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GENERAL CONDITIONS

1. **EXISTING DAMAGE.** Terminix is not responsible for the repair of either visible damage (noted on the attached Inspection Graph) or hidden damage existing as of the date of this agreement. Because damage may be present in areas which are inaccessible to visual inspection, Terminix does not guarantee that the damage disclosed on the Inspection Graph represents all of the existing damage as of the date of this agreement.

2. **WATER LEAKAGE.** Water leakage in treated areas, and leakage in interior areas or through the roof or exterior walls of the identified property, may destroy the effectiveness of Terminix's treatment and is conducive to new infestation. Purchaser is responsible for making timely repairs as are necessary to stop the leakage. Upon completion of repairs by Purchaser, Terminix will provide additional treatment to control infestation at Purchaser's expense. If Purchaser elects not to repair said defects or purchase the additional necessary treatment, then Terminix shall have no further obligation under this agreement.

3. **ADDITIONS, ALTERATIONS.** This agreement covers the property identified on the Inspection Graph as of the date of initial treatment. In the event the premises are structurally modified, altered or otherwise changed or if soil is removed or added around the foundation, Purchaser will immediately notify Terminix and will purchase the additional treatment required by the changes incurred. Failure to do so will terminate this agreement automatically. In the event of structure modification, Terminix also reserves the right to adjust the annual extension charge.

4. **NOTICE OF CLAIMS, ACCESS TO PROPERTY.** Any claim under the terms of this agreement must be made immediately in writing to any Terminix office. Terminix is only obligated to perform under this agreement if the Purchaser allows Terminix access to the identified property for any purpose contemplated by this Agreement, including but not limited to reinspection, whether the inspection was requested by the Purchaser or considered necessary by Terminix.

5. **DISCLAIMER.**

A. Terminix's liability under this agreement will be terminated if Terminix is prevented from fulfilling its responsibilities under the terms of this agreement by reason of delays in transportation, shortages of fuel and/or materials, strikes, embargoes, fires, floods, quarantine restrictions, or any other act of God or circumstances or cause beyond the control of Terminix.

B. This agreement does not cover and Terminix will not be responsible for:
(1) Damage resulting from moisture conditions, including but not limited to fungus damage, and/or
(2) Damage resulting from masonry failure or grade alterations.

C. This agreement excludes coverage on formosan termites *(Coptotermes sp.)*.

D. TERMINIX DISCLAIMS ANY LIABILITY FOR SPECIAL, INCIDENTAL OR CONSEQUENTIAL DAMAGES. THE GUARANTEES STATED IN THIS AGREEMENT ARE GIVEN IN LIEU OF ANY OTHER GUARANTEE OR WARRANTIES, EXPRESS OR IMPLIED, INCLUDING ANY WARRANTY OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE.

6. **CHANGE IN LAW.** Terminix performs its services in accordance with the requirements of federal, state and local law. In the event of a change in existing law as it pertains to the services promised herein, Terminix reserves the right to revise the annual extension charge or terminate this agreement.

7. **NON-PAYMENT, DEFAULT.** In case of non-payment or default by the Purchaser, Terminix has the right to terminate this agreement and reasonable attorney's fees and cost of collection shall be paid by Purchaser, whether suit is filed or not. In addition, interest at the highest legal rate will be assessed for the period of delinquency.

8. **ENTIRE AGREEMENT.** The Service Order signed at the time of purchase, the Agreement and the Inspection Graph constitute the entire agreement between the parties and no other representations or statements will be binding upon the parties.

9. **ARBITRATION.** The Purchaser and Terminix agree that any controversy or claim between them arising out of or relating to the interpretation, performance or breach of any provision of this agreement shall be settled exclusively by arbitration. Such arbitration shall be conducted in accordance with the Commercial Arbitration Rules then in force of the American Arbitration Association before three arbitrators appointed by the American Arbitration Association. The arbitration award shall be final and binding on both parties. Judgment upon such arbitration award may be entered in any court having jurisdiction.

10. **SEVERABILITY.** If any part of this agreement is held to be invalid or unenforceable for any reason, the remaining terms and conditions of this agreement shall remain in full force and effect.

IN THE CIRCUIT COURT
OF BALDWIN COUNTY, ALABAMA

Civil Action Number: CV-91-796

G. MICHAEL DOBSON and WANDA C. DOBSON,
Plaintiffs,

vs.

THE TERMINIX INTERNATIONAL COMPANY, L.P.,
TERMINIX SERVICE, STEVEN C. GWIN, and JAN A. GWIN,
Defendants.

AFFIDAVIT OF W. BRUCE ALVERSON IN SUPPORT OF MOTION BY DEFENDANTS, ALLIED-BRUCE TERMINIX COMPANIES, INC., D/B/A TERMINIX SERVICE AND TERMINIX INTERNATIONAL COMPANY, L.P., FOR STAY PENDING ARBITRATION AND FOR ORDER COMPELLING ARBITRATION

[Filed Aug. 14, 1992]

STATE OF ALABAMA:

COUNTY OF MOBILE:

Before me, the undersigned Notary Public in and for said State and County, personally appeared W. Bruce Alverson, who being by me first duly sworn, on oath deposes and says as follows:

1. My name is W. Bruce Alverson, and I am over the age of twenty-one (21) years. I serve as Eastern Zone Vice President for Defendant Allied-Bruce Terminix Companies, Inc., d/b/a Terminix Service (hereinafter referred to as "Terminix Service"). In such capacity, I have custody and access to the records of said corporation pertain-

ing to the claims involved in this suit and personal knowledge of the matters hereinafter set forth.

2. Defendant Terminix Service is a corporation organized under the laws of the State of Arkansas with offices located in the states of Florida, Georgia, Alabama, Mississippi, Louisiana, Arkansas, Oklahoma and Texas. A true and correct copy of the service order and termite protection plan issued by Defendant Terminix Service to Defendant Steven C. Gwin and subsequently assigned to Plaintiff G. Michael Dobson are attached hereto marked Exhibits "A" and "B" respectively and made a part thereof for all purposes and expressly incorporated by reference as if fully restated herein. Most of the materials and equipment including specifically the chemical used to treat the home involved in this suit were purchased by Defendant Terminix Service outside of the State of Alabama and transferred to the State of Alabama for use on the home.

3. The facts stated in this Affidavit are true and correct. In verification of the truth of said facts and the truth of this Affidavit, my signature is subscribed hereto.

4. Further, Affiant sayeth not.

/s/ W. Bruce Alverson
W. BRUCE ALVERSON
Eastern Zone Vice President for
Allied-Bruce Terminix
Companies, Inc.,
d/b/a Terminix Service

Sworn to and subscribed before me on this the 12th day of August, 1992.

/s/ T. Julian Motes
NOTARY PUBLIC

My Commission Expires:
11-7-92

/s/ T. Julian Motes
JOSEPH P. JONES, JR.
T. JULIAN MOTES
Attorneys for Defendants,
Terminix International
Company, L.P. and
Allied-Bruce Terminix
Companies, Inc., d/b/a
Terminix Service

OF COUNSEL:

SIROTE & PERMUTT, P.C.
One St. Louis Centre, Suite 1000
Post Office Drawer 2025
Mobile, Alabama 36652

CERTIFICATE OF SERVICE

I do hereby certify that I have on this 13th day of August, 1992, served a copy of the foregoing pleading on:

Allan R. Chason, Esq.
Chason & Chason, P.C.
Post Office Box 100
Bay Minette, Alabama 36507

George R. Irvine, III, Esq.
Stone, Granade, Crosby & Blackburn
Post Office Drawer 1509
Bay Minette, Alabama 36507

Mark A. Newell, Esq.
Barker & Janecky, P.C.
Post Office Box 2987
Mobile, Alabama 36652

by mailing a copy of same via United States mail, properly addressed and first class postage prepaid.

/s/ T. Julian Motes

TERMINIX INTERNATIONAL, INC.

NOTE TO CUSTO 27

This is a service order and copy of the Termite Protection Plan. The official Termite Protection Plan will be mailed to you when the work is completed and Terminix has been paid in full.

TERMITE PROTECTION PLAN

PURCHASER Steve Flynn TELEPHONE _____

MAIL ADDRESS 114 Felix Ave

CITY Fairhope STATE Ala ZIP CODE _____

DESCRIPTION OF PROPERTY Res

PROPERTY ADDRESS SAME

CITY Fairhope STATE Ala ZIP CODE _____

Effective 8-25-87 through 8-25-88 for the sum of $ 585.00 Terminix will provide the necessary service to protect the identified property against the attack of subterranean termites *(Reticulitermes sp., Heterotermes sp.)*.

Terminix will extend protection annually to the original owner for the LIFETIME of the identified property subject to the general conditions of this agreement for $ 65.87 per year payable on or before the end of the previous protection period. After the third year and each year thereafter, Terminix reserves the right to revise the annual extension charge. After this Plan is renewed beyond the initial contract term, Terminix will periodically reinspect the identified property and any further treatment found necessary will be performed free.

In the event of additions or alterations to the identified property, Purchaser must arrange with Terminix for additional service which may require an adjustment to the annual extension charge.

This Plan provides protection against new subterranean termite damage to the structure and contents. If new damage occurs during the contract term, Terminix will, upon notification and inspection, arrange for the necessary repairs and pay the cost of labor and materials not to exceed $100,000. New damage is damage associated with an active termite infestation. Unless live termites are found in the damaged area, the damage discovered is old damage and not covered under this Plan.

This protection plan and/or any extension thereof will be effective only upon payment of the charges as provided herein.

Any additional provisions attached hereto including the general conditions and arbitration provision on the reverse side and the inspection graph dated -0- are part of this plan.

Upon transfer of ownership of the identified property, protection against subterranean termites may be continued upon the request of the new owner and upon payment of a contract transfer fee of $ _____. In addition, Terminix reserves the right to revise the annual extension charge upon transfer of ownership. In the event the new owner fails to request continued coverage or does not agree to pay the transfer fee or the revised annual extension charge, the Termite Protection Plan will terminate automatically as of the date of the change of ownership.

NOTICE: YOU, THE PURCHASER, MAY CANCEL THIS TRANSACTION AT ANY TIME PRIOR TO MIDNIGHT OF THE THIRD BUSINESS DAY AFTER THE DATE OF THIS TRANSACTION. SEE THE ATTACHED NOTICE OF CANCELLATION FOR AN EXPLANATION OF THIS RIGHT.

PURCHASER Steve & Flynn DATE 8-25-87

TERMINIX REPRESENTATIVE Edward Lack DATE _____

TERMINIX ADDRESS P.O. Box 1830 TELEPHONE _____

CITY Enfield STATE Ala ZIP CODE _____

SERVICE MANAGER

KEY #33069 / 3-85 RP 0/9[illegible] ...tional, Inc. 1988

DEFENDANT'S EXHIBIT [illegible] A

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GENERAL CONDITIONS

1. **EXISTING DAMAGE.** Terminix is not responsible for the repair of either visible damage (noted on the attached Inspection Graph) or hidden damage existing as of the date of this agreement. Because damage may be present in areas which are inaccessible to visual inspection, Terminix does not guarantee that the damage disclosed on the Inspection Graph represents all of the existing damage as of the date of this agreement.

2. **WATER LEAKAGE.** Water leakage in treated areas, and leakage in interior areas or through the roof or exterior walls of the identified property, may destroy the effectiveness of Terminix's treatment and is conducive to new infestation. Purchaser is responsible for making timely repairs as are necessary to stop the leakage. Upon completion of repairs by Purchaser, Terminix will provide additional treatment to control infestation at Purchaser's expense. If Purchaser elects not to repair said defects or purchase the additional necessary treatment, then Terminix shall have no further obligation under this agreement.

3. **ADDITIONS, ALTERATIONS.** This agreement covers the property identified on the Inspection Graph as of the date of initial treatment. In the event the premises are structurally modified, altered or otherwise changed or if soil is removed or added around the foundation, Purchaser will immediately notify Terminix and will purchase the additional treatment required by the changes incurred. Failure to do so will terminate this agreement automatically. In the event of structure modification, Terminix also reserves the right to adjust the annual extension charge.

4. **NOTICE OF CLAIMS, ACCESS TO PROPERTY.** Any claim under the terms of this agreement will be made immediately in writing to any Terminix office. Terminix is only obligated to perform under this agreement provided the Purchaser allows Terminix access to the identified property for any purpose contemplated by this Contract, including but not limited to reinspection, whether the inspection was requested by the Purchaser or considered necessary by Terminix.

5. **DISCLAIMER.**

A. Terminix's liability under this agreement will be terminated if Terminix is prevented from fulfilling its responsibilities under the terms of this agreement by reason of delays in transportation, shortages of fuel and/or materials, strikes, embargoes, fires, floods, quarantine restrictions, or any other act of God or circumstances or cause beyond the control of Terminix.

B. This agreement does not cover and Terminix will not be responsible for:
   (1) Damage resulting from moisture conditions, including but not limited to fungus damage, and/or
   (2) Damage resulting from masonry failure or grade alterations.

C. This agreement excludes coverage on formosan termites *(Coptotermes sp.)*

D. TERMINIX DISCLAIMS ANY LIABILITY FOR SPECIAL, INCIDENTAL OR CONSEQUENTIAL DAMAGES. THE GUARANTEES STATED IN THIS AGREEMENT ARE GIVEN IN LIEU OF ANY OTHER GUARANTEE OR WARRANTIES, EXPRESS OR IMPLIED, INCLUDING ANY WARRANTY OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE.

6. **CHANGE IN LAW.** Terminix performs its services in accordance with the requirements of federal, state and local law. In the event of a change in existing law as it pertains to the services promised herein, Terminix reserves the right to revise the annual extension charge or terminate this agreement.

7. **NON-PAYMENT, DEFAULT.** In case of non-payment or default by the Purchaser, Terminix has the right to terminate this agreement and reasonable attorney's fees and cost of collection shall be paid by Purchaser, whether suit is filed or not. In addition, interest at the highest legal rate will be assessed for the period of delinquency.

8. **ENTIRE AGREEMENT.** The Service Order signed at the time of purchase, the Agreement and the Inspection Graph constitute the entire agreement between the parties and no other representations or statements will be binding upon the parties.

9. **ARBITRATION.** The Purchaser and Terminix agree that any controversy or claim between them arising out of or relating to the interpretation, performance or breach of any provision of this contract which relates to new termite damage, as defined in this Agreement or the above Plan, shall be settled exclusively by arbitration. Such arbitration shall be conducted in accordance with the Commercial Arbitration Rules of the American Arbitration Association before three arbitrators appointed by the American Arbitration Association. The arbitration award shall be final and binding on both parties. Judgment upon such arbitration award may be entered in any court having jurisdiction. If any part of this provision or if this provision is held to be invalid or unenforceable for any reason, the remaining terms and conditions of this contract shall remain in full force and effect. Claims relating to payment disputes shall not be subject to arbitration.

CONTRACT-CURRENT THRU 8/91

KEY #33073,REV

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TERMINIX INTERNATIONAL

THE TERMINIX INTERNATIONAL COMPANY L.P.

TERMITE PROTECTION PLAN

GUARANTEE NO. PR 08870291-08

C
011-02
632F

TRANSFERRED TO: G Michael Dobson

PURCHASER Steve GWin TELEPHONE

MAIL ADDRESS 114 Fels

CITY Fairhope, STATE Al ZIP CODE 36532

DESCRIPTION OF PROPERTY Residence

PROPERTY ADDRESS

CITY STATE ZIP CODE

Effective 8/25/87 through 8/14/88, for the sum of $ 585.87 Terminix will provide the necessary service to protect the identified property against the attack of subterranean termites *(Reticulitermes sp., Heterotermes sp.)*.

Terminix will extend protection annually to the original owner for the LIFETIME of the identified property subject to the general conditions of this agreement for $ 65.87 per year payable on or before the end of the previous protection period. After the third year and each year thereafter, Terminix reserves the right to revise the annual extension charge. After this Plan is renewed beyond the initial contract term, Terminix will periodically reinspect the identified property and any further treatment found necessary will be performed free.

In the event of additions or alterations to the identified property, Purchaser must arrange with Terminix for additional service which may require an adjustment to the annual extension charge.

This Plan provides protection against new subterranean termite damage to the structure and contents. If new damage occurs during the contract term, Terminix will, upon notification and inspection, arrange for the necessary repairs and pay the cost of labor and materials not to exceed $100,000. New damage is damage associated with an active termite infestation. Unless live termites are found in the damaged area, the damage discovered is old damage and not covered under this Plan.

Upon transfer of ownership of the identified property, protection against subterranean termites may be continued upon the request of the new owner and upon payment of a contract transfer fee of $ 25.00. In addition, Terminix reserves the right to revise the annual extension charge upon transfer of ownership. In the event the new owner fails to request continued coverage or does not agree to pay the transfer fee or the revised annual extension charge, the Termite Protection Plan will terminate automatically as of the date of this change of ownership.

Any additional provisions attached hereto including the general conditions and arbitration provision on the reverse side and the inspection graph dated 8/25/87 are part of this plan.

THE TERMINIX INTERNATIONAL COMPANY L.P. hereby guarantees the fulfillment of the terms of this Plan.

Carlon H Carter

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BY
TERMINIX MANAGER

EXECUTED AT MEMPHIS, TENNESSEE

DEFENDANT'S EXHIBIT B

KEY #33073 REV. 4/87 © The Terminix International Company L.P., 1987

ORIGINATING OFFICE COPY

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GENERAL CONDITIONS

1. **EXISTING DAMAGE.** Terminix is not responsible for the repair of either visible damage (noted on the attached Inspection Graph) or hidden damage existing as of the date of this agreement. Because damage may be present in areas which are inaccessible to visual inspection, Terminix does not guarantee that the damage disclosed on the Inspection Graph represents all of the existing damage as of the date of this agreement.

2. **WATER LEAKAGE.** Water leakage in treated areas, and leakage in interior areas or through the roof or exterior walls of the identified property, may destroy the effectiveness of Terminix's treatment and is conducive to new infestation. Purchaser is responsible for making timely repairs as are necessary to stop the leakage. Upon completion of repairs by Purchaser, Terminix will provide additional treatment to control infestation at Purchaser's expense. If Purchaser elects not to repair said defects or purchase the additional necessary treatment, then Terminix shall have no further obligation under this agreement.

3. **ADDITIONS, ALTERATIONS.** This agreement covers the property identified on the Inspection Graph as of the date of initial treatment. In the event the premises are structurally modified, altered or otherwise changed or if soil is removed or added around the foundation, Purchaser will immediately notify Terminix and will purchase the additional treatment required by the changes incurred. Failure to do so will terminate this agreement automatically. In the event of structure modification, Terminix also reserves the right to adjust the annual extension charge.

4. **NOTICE OF CLAIMS, ACCESS TO PROPERTY.** Any claim under the terms of this agreement must be made immediately in writing to any Terminix office. Terminix is only obligated to perform under this agreement if the Purchaser allows Terminix access to the identified property for any purpose contemplated by this Agreement, including but not limited to reinspection, whether the inspection was requested by the Purchaser or considered necessary by Terminix.

5. **DISCLAIMER.**

A. Terminix's liability under this agreement will be terminated if Terminix is prevented from fulfilling its responsibilities under the terms of this agreement by reason of delays in transportation, shortages of fuel and/or materials, strikes, embargoes, fires, floods, quarantine restrictions, or any other act of God or circumstances or cause beyond the control of Terminix.

B. This agreement does not cover and Terminix will not be responsible for:
   (1) Damage resulting from moisture conditions, including but not limited to fungus damage, and/or
   (2) Damage resulting from masonry failure or grade alterations.

C. This agreement excludes coverage on formosan termites *(Coptotermes sp.)*.

D. TERMINIX DISCLAIMS ANY LIABILITY FOR SPECIAL, INCIDENTAL OR CONSEQUENTIAL DAMAGES. THE GUARANTEES STATED IN THIS AGREEMENT ARE GIVEN IN LIEU OF ANY OTHER GUARANTEE OR WARRANTIES, EXPRESS OR IMPLIED, INCLUDING ANY WARRANTY OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE.

6. **CHANGE IN LAW.** Terminix performs its services in accordance with the requirements of federal, state and local law. In the event of a change in existing law as it pertains to the services promised herein, Terminix reserves the right to revise the annual extension charge or terminate this agreement.

7. **NON-PAYMENT, DEFAULT.** In case of non-payment or default by the Purchaser, Terminix has the right to terminate this agreement and reasonable attorney's fees and cost of collection shall be paid by Purchaser, whether suit is filed or not. In addition, interest at the highest legal rate will be assessed for the period of delinquency.

8. **ENTIRE AGREEMENT.** The Service Order signed at the time of purchase, the Agreement and the Inspection Graph constitute the entire agreement between the parties and no other representations or statements will be binding upon the parties.

9. **ARBITRATION.** The Purchaser and Terminix agree that any controversy or claim between them arising out of or relating to the interpretation, performance or breach of any provision of this agreement shall be settled exclusively by arbitration. Such arbitration shall be conducted in accordance with the Commercial Arbitration Rules then in force of the American Arbitration Association before three arbitrators appointed by the American Arbitration Association. The arbitration award shall be final and binding on both parties. Judgment upon such arbitration award may be entered in any court having jurisdiction.

10. **SEVERABILITY.** If any part of this agreement is held to be invalid or unenforceable for any reason, the remaining terms and conditions of this agreement shall remain in full force and effect.

IN THE CIRCUIT COURT
OF BALDWIN COUNTY, ALABAMA

(Title Omitted in Printing)

AFFIDAVIT OF DANIEL F. JOHNSON IN SUPPORT OF MOTION BY DEFENDANTS, ALLIED-BRUCE TERMINIX COMPANIES, INC., D/B/A TERMINIX SERVICE AND TERMINIX INTERNATIONAL COMPANY, L.P., FOR STAY PENDING ARBITRATION AND FOR ORDER COMPELLING ARBITRATION

[Filed Aug. 14, 1992]

STATE OF TENNESSEE:

COUNTY OF SHELBY:

Before me, the undersigned Notary Public in and for said State and County, personally appeared Daniel F. Johnson, who being by me first duly sworn, on oath deposes and says as follows:

1. My name is Daniel F. Johnson and I am over the age of twenty-one (21) years. I serve as Corporate Counsel for Defendant The Terminix International Company L.P. (hereinafter referred to as "Terminix International"). In such capacity, I have custody and access to the records of said company pertaining to the claims involved in this suit and personal knowledge of the matters hereinafter set forth.

2. Defendant Terminix International is a limited partnership organized under the laws of a State other than Alabama and with its principal place of business located in Memphis, Tennessee. Defendant Terminix International has offices located outside the State of Alabama,

and the general partner and limited partner of said Defendant are companies that have their principal places of business outside the State of Alabama.

3. A true and correct copy of the Termite Protection Plan (the "Plan") issued by Defendant Allied-Bruce Terminix Companies, Inc., d/b/a Terminix Service (hereinafter referred to as "Terminix Service") to Defendant Steven C. Gwin and subsequently assigned to Plaintiff G. Michael Dobson is attached hereto marked Exhibit "A" and made a part thereof for all purposes and expressly incorporated by reference as if fully restated herein. As shown by the terms of the Plan, Defendant Terminix International guarantees the fulfillment of the terms of the Plan.

4. The facts stated in this Affidavit are true and correct. In verification of the truth of said facts and the truth of this Affidavit, my signature is subscribed hereto.

5. Further, Affiant sayeth not.

/s/ Daniel F. Johnson
DANIEL F. JOHNSON
Corporate Counsel for
The Terminix International
Company L.P.

(Notary and Certificate of Service Omitted in Printing)

(Exhibit A Appears at pp. 75-78)

IN THE CIRCUIT COURT
OF BALDWIN COUNTY, ALABAMA

(Title Omitted in Printing)

MOTION OF DEFENDANTS, ALLIED-BRUCE TERMINIX COMPANIES, INC., D/B/A TERMINIX SERVICE AND TERMINIX INTERNATIONAL COMPANY, L.P., FOR STAY PENDING ARBITRATION AND FOR ORDER COMPELLING ARBITRATION

[Filed Aug. 14, 1992]

COME NOW, Allied-Bruce Terminix Companies, Inc., d/b/a Terminix Service ("Terminix Service") and Terminix International Company, L.P. ("Terminix International"), Defendants in the above-styled action, and move the Court for a stay of this action pending arbitration of the claims asserted by Plaintiffs, G. Michael Dobson and Wanda C. Dobson (hereinafter referred to collectively as "Dobson"), against Defendants, Terminix Service and Terminix International, and of the cross-claims asserted by Defendants, Steven C. Gwin and Jan A. Gwin (hereinafter referred to collectively as "Gwin"), against Defendants, Terminix Service and Terminix International, and for an order compelling the parties to arbitrate these claims. In support of this request, Defendants, Terminix Service and Terminix International, would offer the following:

1. Plaintiffs Dobson filed the present action against Defendants, Terminix Service and Terminix International, for alleged fraudulent misrepresentations concerning a visual inspection of a home purchased by Plaintiffs from Defendants Gwin and for an alleged negligent inspection

of the same. Plaintiffs Dobson also sued Defendants Gwin for alleged misrepresentations and for alleged fraudulent concealment relating to the same home.

2. Defendants filed answers to Plaintiffs' complaint denying the material allegations of the same and asserting several affirmative defenses. The parties proceeded with some discovery in this matter.

3. Plaintiffs Dobson recently filed their first amended complaint asserting for the first time an agency relationship between Defendant Terminix Service and Defendant Terminix International, a claim for punitive damages and a claim for breach of the termite protection plan issued by Defendant Terminix Service to Defendants Gwin and subsequently assigned to Plaintiffs Dobson. Defendants Gwin also recently filed a cross-claim asserting for the first time claims seeking affirmative relief from Defendants, Terminix Service and Terminix International. The cross-claim includes two counts consisting of a claim for breach of the termite protection plan originally issued by Defendant Terminix Service to Defendants Gwin and a claim for negligent inspections, treatments and performance of the contractual duties contained in the termite protection plan.

4. The termite protection plan made the basis of the claims asserted by Plaintiffs Dobson and Defendants Gwin against Defendants, Terminix Service and Terminix International, contains the following provision:

> The Purchaser and Terminix agree that any controversy or claim between them arising out of or relating to the interpretation, performance or breach of any provision of this agreement shall be settled exclusively by arbitration. Such arbitration shall be conducted in accordance with the Commercial Arbitration Rules then in force of the American Arbitration Association before three arbitrators appointed by the American Arbitration Association. The arbitration award shall be final and binding on

> both parties. Judgment upon such arbitration award may be entered in any court having jurisdiction.

The broad language of this arbitration provision shows that the parties to this contract agreed to submit any claims arising from the relationship established between the parties as a result of this agreement to arbitration and that the parties would be bound by any award issued out of such arbitration proceedings.

5. The Congress of the United States passed the Federal Arbitration Act in part to reverse centuries of judicial hostility to arbitration agreements and to place arbitration agreements upon the same footing as other contracts. *Moses H. Cone Memorial Hospital v. Mercury Construction Co.*, 460 U.S. 1, 24-25 (1983); *A. G. Edwards & Sons, Inc. v. Clark*, 558 So.2d 358, 361 (Ala. 1990). If an agreement to arbitrate a dispute comes within the provisions of the Federal Arbitration Act, Alabama courts will enforce that agreement in accordance with the federal policy as expressed in the Act and the court decisions construing the same. *Ex parte McKinney*, 515 So.2d 693, 698 (Ala. 1987). The provisions of the Federal Arbitration Act, if applicable, serve to preempt any state law purporting to deny the enforcement of a predispute arbitration agreement and provides for the enforcement of the arbitration agreement. *Ex parte Brice Building Co., Inc.*, 26 A.B.R. 4250, 4253 (Ala. July 17, 1992).

6. Section 2 of the Federal Arbitration Act provides in part as follows:

> A written provision in . . . a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction or the refusal to perform the whole or any part thereof, . . . shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or at equity for the revocation of any contract.

9 U.S.C. Section 2 (1947). Section 1 of the Federal Arbitration Act defines commerce very broadly to include commerce among the several states. 9 U.S.C. Section 1 (1947). Section 3 of the Federal Arbitration Act directs any court in the United States to stay an action pending arbitration if the action brought before that court includes any issue referable to arbitration under the terms of the Act. 9 U.S.C. Section 3 (1974).

7. The Alabama courts have found the Federal Arbitration Act to be applicable when there is a written contract containing an arbitration provision and when the contract involves interstate commerce. *Ex parte Brice Building Co., Inc.*, 26 A.B.R. 4250, 4253 (Ala. July 17, 1992); *Ex parte Shamrock Food Service, Inc.*, 514 So.2d 921 (Ala. 1987); *Ex parte Costa and Head (Atrium), Ltd.*, 486 So.2d 1272, 1275 (Ala. 1986). In the context of construction cases, Alabama courts have construed the requirement of interstate commerce very broadly so that the slightest nexus of the agreement with interstate commerce will bring the agreement within the Federal Arbitration Act. *Ex parte Brice Building Co., Inc.*, 26 A.B.R. at 4254-4257; *Ex parte Costa and Head (Atrium), Ltd.*, 486 So.2d at 1275. In these cases, the construction was to be totally performed within the State of Alabama, but the courts still found the Federal Arbitration Act to be applicable because of the involvement of interstate commerce.

8. In the *Costa* case, the court found the following facts sufficient to support a finding of an involvement of interstate commerce: when one of the parties is a limited partnership with partners outside the State of Alabama, when the principal place of business of one of the parties is outside the State of Alabama, and when part of the materials incorporated into the project came from outside the State of Alabama and are transported into Alabama. *Ex parte Costa and Head (Atrium), Ltd.*, 486 So.2d at 1275. In the *Brice* case, the contract involved an

Alabama plaintiff and Alabama defendants with the contract negotiated and to be executed in the State of Alabama, but the court still found the Federal Arbitration Act to be applicable because of the use of out-of-state building materials and possibly an out-of-state subcontractor to perform part of the work. *Ex parte Brice Building Co., Inc.*, 26 A.B.R. at 4256. Even though the connection with interstate commerce in the *Brice* case was found to be tenuous by the Alabama Supreme Court, the court found the same to be sufficient to invoke the provisions of the Federal Arbitration Act. *Id.*

9. In the context of the purchase of a consumer good within the State of Alabama, the Alabama Supreme Court has enunciated a little different standard as far as the requirement of interstate commerce to invoke the Federal Arbitration Act. *Ex parte Williams*, 555 So.2d 146 (Ala. 1989); *Ex parte Warren*, 548 So.2d 157 (Ala. 1989). In these cases, an Alabama resident had purchased an automobile from a Alabama dealership with offices only within the State of Alabama and the only connection with interstate commerce was the fact that the automobile had been manufactured outside the State of Alabama. *Ex parte Williams*, 555 So.2d at 148; *Ex parte Warren*, 548 So.2d at 159-160. The courts in these narrow fact situations considered whether the parties at the time that they entered into these contracts contemplated substantial interstate activity. *Ex parte Warren*, 548 So.2d at 159-160. The court in the *Warren* case also found that the facts of that case did not meet the standard established for interstate commerce in the *Costa* case.

10. The Alabama Supreme Court has found that the standard followed in the *Warren* and *Williams* cases is strictly limited to the narrow factual context found in these cases. *Ex parte Brice Building Co., Inc.*, 26 A.B.R. at 4255-4256. However, the facts of the present case supporting the involvement of interstate commerce clearly meet the standards enunciated in either *Costa* or *Warren.*

11. The affidavit of W. Bruce Alverson establishes that Defendant Terminix Service, a corporation organized under the laws of the State of Arkansas, has offices located in several states and that a large portion of the materials and equipment used to treat the home involved in this suit, including specifically the chemical, were purchased outside the State of Alabama by said Defendant and transported into this state. The affidavit of Daniel F. Johnson shows that Defendant Terminix International is a limited partnership organized under the laws of a state other than Alabama and that its principal place of business is located in Memphis, Tennessee. This affidavit also establishes that Defendant Terminix International has offices located outside the State of Alabama and that the general partner and limited partner of said Defendant are located outside this state. The termite protection plan made the basis of the claims asserted by Plaintiffs Dobson and Defendants Gwin was issued by Defendant Terminix Service, and the same was guaranteed by Defendant Terminix International.

12. These facts show substantial interstate activity as enunciated in the *Warren* case and establish the significant connections that the termite protection plan involved in this case has with interstate commerce. The termite protection plan made the basis of the claims asserted by Plaintiffs Dobson and Defendants Gwin against Defendants, Terminix Service and Terminix International, clearly involves interstate commerce, and the Federal Arbitration Act is applicable to this written contract which calls for arbitration of any claim between the parties arising out of or relating to the agreement. If a written contract containing an arbitration clause comes within the provisions of the Federal Arbitration Act, a court must stay its proceedings if it is satisfied that an issue brought before it is arbitrable under the agreement. *Ex parte Shamrock Food Service, Inc.*, 514 So.2d 921, 922 (Ala. 1987).

13. After a court determines that a written agreement containing an arbitration clause comes within the provi-

sions of the Federal Arbitration Act, the court then must decide what issues involved in the suit before the court are arbitrable. *A.G. Edwards & Sons, Inc. v. Clark*, 558 So.2d 358, 361 (Ala. 1990) (quoting *Morgan v. Smith Barney Harris Upham & Co.*, 729 F.2d 1163, 1165 (8th Cir. 1984) and *Moses H. Cone Memorial Hospital v. Mercury Construction Co.*, 460 U.S. 1, 24-25 (1983)). The determination of the scope of an arbitration provision included in a contract is a matter for the court. *Explo, Inc. v. Southern Natural Gas Co.*, 788 F.2d 1096, 1098 (5th Cir. 1986); *Ex parte Warrior Basin Gas Co.*, 512 So.2d 1364, 1370 (Ala. 1987).

14. If a court cannot find with *positive assurance* that an arbitration clause coming within the terms of the Federal Arbitration Act was intended to exclude a claim asserted in a suit, then the court should stay the action pending arbitration and order the parties to submit the claim made the basis of the suit to arbitration. *Ex parte Warrior Basin Gas Co.*, 512 So.2d 1364, 1370 (Ala. 1987) (Emphasis added). Any doubts as to whether a claim involved in a suit comes within the provisions of an arbitration clause should be resolved in favor of arbitration. *Neal v. Hardee's Food Systems, Inc.*, 918 F.2d 34, 37 (5th Cir. 1990); *Ex parte Shamrock Food Service, Inc.*, 514 So.2d 921, 922 (Ala. 1987). In the *Neal* case, the Fifth Circuit Court of Appeals found claims for fraud, deception, bad practices, breach of contract and breach of good faith subject to arbitration pursuant to a broad arbitration clause included in a general agreement establishing the relationship between the parties. *Neal*, 918 F.2d at 38.

15. Alabama courts and Federal courts have found broad arbitration clauses to encompass tort claims asserted between parties to written agreements, and the courts have not allowed parties to escape their agreements to arbitrate matters by sounding their claims in tort. *McBro Planning and Development Co. v. Triangle Electrical Construction Co., Inc.*, 741 F.2d 342, 344 (11th

Cir. 1984); *see Ex parte Costa and Head (Atrium), Ltd.*, 486 So.2d 1272, 1276 (Ala. 1986). The joinder of arbitrable claims with claims between other parties which are not arbitrable will not prevent a court from staying an action and directing the parties to arbitrate the claims covered by the written agreement. *Ex parte McKinney*, 515 So.2d 693, 701 (Ala. 1987) (citing *Dean Witter Reynolds, Inc. v. Byrd*, 470 U.S. 213 (1985)). A trial court has no discretion to deny arbitration on the grounds of judicial economy, possible inconsistent results or the existence of non-arbitrable claims. *Ex parte Costa and Head (Atrium), Ltd.*, 486 So.2d 1272, 1276 (Ala. 1986).

16. The arbitration clause contained in the termite protection plan involved in the present suit is very broad and covers any controversy or claim between the parties arising out of or relating to the written agreement between the parties. The claims asserted by Plaintiffs Dobson in this suit against Defendants, Terminix Service and Terminix International, arise out of or relate to the termite protection plan containing the arbitration clause.

17. Plaintiffs Dobson have asserted against Defendants, Terminix Service and Terminix International, claims for alleged breach of the termite protection plan, for alleged fraudulent misrepresentation concerning a visual inspection of the home involved in this suit which was performed free of cost because of the existence of the termite protection plan, and alleged negligent inspection of the home during the visual inspection performed as part of the termite protection plan. Clearly, the claim for breach of the termite protection plan asserted against Defendants, Terminix Service and Terminix International, by Plaintiffs Dobson comes within the language of the arbitration clause contained in the agreement. Even though the other two claims sound in tort, the same arise out of or relate to the agreement between the parties because the inspection was performed free of charge by Defendant Terminix Service due to the existence of the

termite protection plan. (See deposition of George Walter Adkison, page 41, and deposition of William Daniel Calhoun, page 20).

18. The broad language contained in the arbitration clause prevents this Court from finding with positive assurance that the tort claims asserted by Plaintiffs Dobson against Defendants, Terminix Service and Terminix International, were intended to be excluded from the coverage of the clause. Any doubts as to the coverage of the arbitration clause should be construed in favor of arbitration, and Plaintiffs Dobson should be required to submit all claims asserted against Defendants, Terminix Service and Terminix International, to arbitration. Plaintiffs Dobson are parties to a written agreement containing an arbitration clause which is very broad and which encompasses all claims asserted by Plaintiffs.

19. As far as the cross-claim asserted by Defendants Gwin, these claims clearly come within the broad language of the arbitration clause included in the termite protection plan originally issued to Defendants Gwin by Defendant Terminix Service. Defendants Gwin assert two claims against Defendants, Terminix Service and Terminix International, for breach of contract and for negligent inspections, treatments and performance of contractual duties. Even though one of these claims sounds in tort, the contractual duties made the basis of the negligence claim arise out of the obligations included in the termite protection plan containing the arbitration clause. Again, this Court cannot find with positive assurance that the broad language of the arbitration clause included in the termite protection plan was intended to exclude the claims asserted by Defendants Gwin against Defendants, Terminix Service and Terminix International. These claims are clearly governed by the broad language of the arbitration clause included in the written agreement between the parties.

20. The Federal Arbitration Act is applicable to the termite protection plan involved in this suit due to the

interstate connections of Defendants, Terminix Service and Terminix International. The tort and contract claims asserted by Plaintiffs Dobson and Defendants Gwin against Defendants, Terminix Service and Terminix International, clearly arise out of or relate to the termite protection plan or the duties arising out of the same. If this Court considers the broad language of the arbitration clause included in the written agreement between the parties to this suit and resolves any doubt as to the scope of this clause in favor of arbitration, then the Court should stay this action pending arbitration of all claims asserted by Plaintiffs Dobson and Defendants Gwin against Defendants, Terminix Service and Terminix International, and should order the parties to arbitrate these claims.

WHEREFORE, Defendants, Terminix Service and Terminix International, move the Court for the entry of an order staying this action pending arbitration of the claims asserted by Plaintiffs Dobson and Defendants Gwin against Defendants, Terminix Service and Terminix International, and for the entry of an order compelling Plaintiffs Dobson and Defendants Gwin to arbitrate all claims asserted in this suit against Defendants, Terminix Service and Terminix International. Defendants, Terminix Service and Terminix International, request such other relief as the Court deems appropriate.

/s/ T. Julian Motes
JOSEPH P. JONES, JR.
T. JULIAN MOTES
Attorneys for Defendants,
Terminix International
Company, L.P. and
Allied-Bruce Terminix
Companies, Inc., d/b/a
Terminix Service

Of Counsel:

SIROTE & PERMUTT, P.C.
One St. Louis Centre, Suite 1000
Post Office Drawer 2025
Mobile, Alabama 36652

ORAL ARGUMENT RESPECTFULLY REQUESTED.

/s/ T. Julian Motes

(Certificate of Service Omitted in Printing)

IN THE CIRCUIT COURT
OF BALDWIN COUNTY, ALABAMA

(Title Omitted in Printing)

BRIEF OF G. MICHAEL DOBSON AND WANDA C. DOBSON IN OPPOSITION TO MOTION TO COMPEL ARBITRATION

[Filed Sep. 1, 1992]

Code of Alabama, Section 8-1-41 (1975), provides as follows:

> The following obligations cannot be specifically enforced:
>
> . . .
>
> (3) an agreement to submit a controversy to arbitration; . . . .

It is undisputed that the law of Alabama is that pre-dispute arbitration agreements are unenforceable. *Ex Parte Brice Building Company, Inc.*, 26 ABR 4250 (July 17, 1992).

On the other hand, the Federal Arbitration Act provides that pre-dispute arbitration provisions contained in contracts involving interstate commerce are enforceable. In all cases, then, the issue is whether or not a particular contract involves interstate commerce such that it is controlled by federal law rather than state law.

In this case, Terminix relies on *Ex Parte Costa and Head (Atrium), Limited,* 486 So.2d 1272 (Ala. 1986). That case involved a multi-million dollar commercial construction project in Alabama. One of the contractors had its principal place of business in Knoxville, Tennessee,

another in Rochester, New York, and another was a limited partnership composed of limited partners from other states outside Alabama. Additionally, subcontractors on the job were incorporated in various states, other than Alabama. Materials incorporated into the project were manufactured in other states and transported into Alabama. Under those facts, the Court held that interstate commerce was sufficiently involved in the transaction so as to allow federal law to preempt Alabama law and apply the Federal Arbitration Act.

It is our contention, however, that the case at hand is substantially different from *Costa*. The facts of this case involve a consumer transaction where an Alabama husband and wife purchased an Alabama residence from another Alabama husband and wife. Incidental to the sale of the home was the assignment to the purchaser of a termite protection plan issued by Terminix Services, another Alabama corporation. The entire transaction took place in Alabama without any out of state involvement.

Terminix, on the other hand, in an effort to find some interstate commerce involved in this purely local transaction, points to the fact that the chemicals which were used in treating termites at the home in Fairhope were purchased outside of Alabama; and the fact that Terminix also has offices outside of Alabama. We submit that this is simply not the same kind of case as *Costa* and that these connections with interstate commerce are too tenuous to justify the finding that federal jurisdiction has preempted very clear state law.

Our position is clearly supported by two decisions of the Alabama Supreme Court. In *Ex Parte Warren,* 548 So.2d 157 (Ala. 1989), cert. den. 110 Sup.Ct. 554, and in *Ex Parte Williams,* 555 So.2d 146 (Ala. 1989), the Supreme Court refused to find sufficient involvement with interstate commerce so as to apply federal law. Both *Warren* and *Williams* involved cases where consumers visited an Alabama car dealership and purchased auto-

mobiles which had been manufactured out of state. In each case, the sales contract included an arbitration clause. When sued over the sales contract, the car dealership attempted to invoke the arbitration clause saying that federal law was controlling because the automobile was manufactured outside of Alabama. In each case, *Costa* was cited by the dealership as authority for applying the Federal Arbitration Act. However, in each case, the Supreme Court refused, holding that

> (a)lthough we note that the language quoted from *Ex Parte Costa and Head* is very broad, we find, nonetheless, that, under the particular facts of this case, the transaction in question does not involve interstate commerce, as contemplated by the FAA; and, therefore, we hold that the provisions of the federal legislation are not controlling. *Warren, supra,* 159.

The Court in *Warren* noted that there was no reason to anticipate that the parties to that transaction had *contemplated* substantial interstate activity.

These cases were all recently analyzed by the Alabama Supreme Court in *Ex Parte Brice Building Company, Inc.*, 26 ABR 4250 (July 17, 1992). That case involved the construction of a mosque in Birmingham for the Zamora Shrine Temple. Obviously, this case involves another commercial construction contract, this time with a Delaware corporation. Importantly, however, that contract specifically called for an ornamental dome which would sit atop the mosque and which was to be fabricated and erected by a company in Torrence, California, and then shipped to Alabama. Under those facts, the Supreme Court held that *Costa* controlled and not *Warren* and that the transaction involved sufficient interstate commerce as to justify federal preemption.

The facts of the Terminix case are very much different, however, from either *Costa* or *Brice*. The distinction between these cases, on the one hand, and *Warren* and

Williams on the other, is clear. Obviously, it does not lie in the fact that there is some remote connection to interstate commerce. After all, practically every transaction in our lives has *some* connection with interstate commerce. The object of the contract in *Warren* and *Williams* was the purchase of an automobile, built in Detroit and shipped to Alabama; and in *Brice* it was the dome of a mosque which was to be built in California and shipped to Alabama. The distinction in these cases, however, obviously involves practical considerations having to do with the contemplation of the parties. In *Brice*, the parties knew that they were involving themselves in a transaction involving interstate commerce. In *Warren* and *Williams*, however, they were simply purchasing an automobile. We submit that the termite protection plan at issue here is more like *Warren* and *Williams* than it is *Brice* and *Costa*. Mike and Wanda Dobson involved themselves in a routine consumer transaction with no notion whatsoever that they might be involved in interstate commerce. The Terminix office was in Daphne and there was no hint of any interstate activity. *Costa* and *Brice*, however, involved large commercial construction contracts where the parties expressly provided for interstate activity. That is the distinction between these lines of cases and for that reason the Alabama prohibition against predispute arbitration agreements is controlling. The Motion to Compel Arbitration should be denied.

Respectfully submitted,

/s/ Allan R. Chason
ALLAN R. CHASON
Attorney for Plaintiffs

Of Counsel:

CHASON & CHASON, P.C.
P.O. Box 100
Bay Minette, Alabama 36507

(Certificate of Service Omitted in Printing)

THE CIRCUIT COURT OF BALDWIN COUNTY

Case No. CV 91-796

G. MICHAEL DOBSON, *et al.*

vs.

THE TERMINIX INTERNATIONAL CO., *et al.*

Motion for order compelling arbitration and for order of stay pending arbitration is denied.

/s/ James H. Reid
Judge

SUPREME COURT OF ALABAMA
SPECIAL TERM, 1993

1920473

ALLIED-BRUCE TERMINIX COMPANIES, INC., *et al.*

v.

G. MICHAEL DOBSON, WANDA C. DOBSON,
STEVEN GWIN, and JAN GWIN

Appeal from Baldwin Circuit Court
(CV-91-796)

ALMON, JUSTICE.

The defendants, Allied-Bruce Terminix Companies, Inc. ("Terminix Service"), and Terminix International Company ("Terminix International") appeal from an order of the trial court denying their motion to compel arbitration of the tort and breach of contract claims filed against them by Michael Dobson, Wanda Dobson, Steven Gwin, and Jan Gwin. The issue for our review is whether the arbitration clause contained in a termite bond is enforceable under the Federal Arbitration Act, 9 U.S.C. § 1 et seq. ("FAA").

In August 1987, Steven Gwin allowed the termite bond on his house in Fairhope, Alabama, to expire, and he purchased a replacement bond from Terminix Service. Terminix Service is an Arkansas corporation that does business in several states, including Alabama, Arkansas,

Florida, Georgia, Mississippi, Louisiana, Oklahoma, and Texas. The bond was guaranteed by Terminix International, a limited partnership that has its principal place of business in Memphis, Tennessee.

In 1991, Steven and Jan Gwin agreed to sell the house to Michael and Wanda Dobson. The sales contract required the Gwins to provide written evidence from a licensed pest control company that the company had performed a visual inspection of the house and had observed no active infestation of termites or damage from active infestation. The contract also required that the termite bond be transferred to the Dobsons at the closing of the sale. Because of the existing bond on the house, Terminix Service agreed to perform the inspection and to issue the required statement. At the closing, the Gwins furnished Dobson with a standard Veterans' Administration ("VA") form; the V.A. form provided that Terminix Service had observed no visible evidence of active infestation during the inspection.

The Dobsons later discovered termite damage to the house, and they brought an action against the Gwins, alleging fraud, and against Terminix Service and Terminix International, alleging fraud in connection with the representations in the V.A. form, and alleging breach of contract. The Gwins cross-claimed against Terminix Service and Terminix International. Terminix Service and Terminix International moved to stay the proceedings and to compel the Dobsons and the Gwins to submit their claims to arbitration pursuant to an arbitration clause in the bond. The trial court denied this motion, and the defendants appeal.

Predispute arbitration agreements are unenforceable under Alabama law. Ala. Code 1975, § 8-1-41. However, if an arbitration agreement is voluntarily entered into and is contained in a contract that involves interstate commerce, then the FAA preempts state law and renders the agreement enforceable. *A.G. Edwards & Sons, Inc.*

v. Syvrud, 597 So. 2d 197 (Ala. 1992). The Terminix companies contend that, because the United States Supreme Court has held in *Southland Corp. v. Keating,* 465 U.S. 1, 104 S.Ct. 852, 79 L.Ed.2d 1 (1984), that Congress's regulatory power under the FAA is co-extensive with its commerce power, this Court should apply the "slightest nexus" standard first enunciated in *Ex parte Costa & Head (Atrium), Ltd.,* 486 So. 2d 1272 (Ala. 1986), to this situation. This standard provides that if the contract in question has the slightest nexus with interstate commerce, the FAA will apply. *Costa & Head*; *Ex parte Brice Building Co.,* 607 So. 2d 132 (Ala. 1992). Terminix Service and Terminix International argue that, because they are out-of-state entities, and because some of the materials used in fulfilling their duties imposed by the termite bond were brought into Alabama from out-of-state, the bond has at least a "slight nexus" with interstate commerce.

We need not address this argument, however, in light of this Court's decision in *Ex parte Jones,* [Ms. 1920249, July 16, 1993] —— So. 2d —— (Ala. 1993).[1] In *Jones,* we explicitly rejected the *Costa & Head* "slightest nexus" standard in favor of the standard enunciated in *Ex parte Warren,* 548 So. 2d 157 (Ala. 1989), cert. denied, 493 U.S. 998, 110 S.Ct. 554, 107 L.Ed.2d 550 (1989). We held:

> "To resolve any inconsistency or confusion generated by the existence of two different standards, and determining, as we now do, that *Warren* represents a more reasoned approach than the *Costa* standard, we overrule any case inconsistent with *Warren,* to the extent that it states a different standard for determining the involvement of interstate commerce."

—— So. 2d at ——. The *Warren* standard, which was invoked in *Warren* to cover only the "narrow" circum-

[1] See also *Continental Grain Co. v. Beasley,* [Ms. 1920241, July 16, 1993] —— So. 2d —— (Ala. 1993).

stances in which Alabama residents had purchased an automobile for consumer purposes from an in-state dealership, was first set forth by Judge Lombard in a special concurrence in *Metro Industrial Painting Corp. v. Terminal Constr. Co.*, 287 F.2d 382 (2d Cir.), cert. denied, 368 U.S. 817, 82 S.Ct. 31, 7 L.Ed.2d 24 (1961):

> "The significant question, therefore [in determining whether a contract evidences a transaction involving commerce], is not whether, in carrying out the terms of the contract, the parties *did* cross state lines, but whether, at the time they entered into it and accepted the arbitration clause, they *contemplated* substantial interstate activity. Cogent evidence regarding their state of mind at the time would be the terms of the contract, and if it, on its face, evidences interstate traffic . . . the contract should come within § 2 [of the FAA.] In addition, evidence as to how the parties expected the contract to be performed and how it was performed is relevant to whether substantial interstate activity was contemplated."

287 F.2d at 387 (emphasis in original).

Terminix Service and Terminix International argue that the bond involves interstate commerce even under the more restrictive *Warren* standard. In addition to the evidence cited above in support of their *Costa & Head* argument, the Terminix companies cite the following in support of their contention that at the time they entered into the contract the parties "contemplated substantial interstate activity": Steven Gwin's testimony that he allowed his bond with a local pest control company to expire so that he could "go with a national company like Terminix"; the fact that the bond instrument showed on its face that it was executed in Memphis, Tennessee; and the fact that the bond contained a statement that it was subject to federal regulation.

A brief survey of cases from other jurisdictions that have applied the standard will be useful in determining

whether the parties contemplated substantial interstate activity when they entered the termite bond.

Several cases applying the *Warren* standard involve contracts for the construction of large projects. In *Burke County Public Schools Board of Educ. v. Shaver Partnership*, 303 N.C. 408, 279 S.E.2d 816 (1981), the North Carolina Supreme Court held that a contract between a North Carolina school board and an Indiana architectural firm for the construction of school buildings did involve interstate commerce so as to be covered by the FAA. In so holding, the Court stated:

> "We do not mean to suggest that where the contracting parties are merely located in different states or where other facts tending only to show diversity of citizenship are present, the contract must necessarily be found to contemplate substantial interstate activity so as to trigger the act's applicability. Where, however, performance of the contract necessarily involves, so that the parties must have contemplated, substantial interstate activity, the contract evidences a transaction involving commerce within the meaning of the [FAA]."

303 N.C. at 418, 279 S.E.2d at 822. The Court then held that the following evidence established that when they entered into the contract the parties contemplated substantial interstate activity: certain contractual provisions called for the Indiana firm to come to the North Carolina building site for various reasons; accounting records on the project were maintained in Kansas; the Indiana firm dealt with suppliers from across the country in performing its contractual duties; and certain design work was performed by a Michigan firm. See also *G.D. Searle & Co. v. Metric Constructors, Inc.*, 572 F.Supp. 836 (N.D. Ga. 1983); *Dimambro-Northend Assocs. v. Blanck-Alvarez, Inc.*, 251 Ga. 704, 309 S.E.2d 364 (1983); *University Casework Systems, Inc. v. Bahre*, 172 Ind. App. 624, 362 N.E.2d 155 (1977).

Some courts have also held the FAA applicable to contracts for the construction of smaller projects. In *R.J. Palmer Constr. Co. v. Wichita Band Instrument Co.*, 7 Kan. App.2d 363, 642 P.2d 127 (1982), the Kansas Court of Appeals held that the FAA applied to a contract for the construction of a music store. The Court held that because the store was to be built out of California redwood, the parties knew that the contract would involve interstate activity.

A smaller number of cases applying the *Warren* standard involve personal service contracts. For example, in *Bennish v. North Carolina Dance Theatre, Inc.*, 108 N.C. App. 42, 422 S.E.2d 335 (1992), the North Carolina Court of Appeals held that a dancer and his employer contemplated substantial interstate activity when they entered the contract, because the contract provided guidelines on air travel and the employer introduced evidence that the dancer toured outside of North Carolina for a substantial amount of the contract period. See also *Erving v. Virginia Squires Basketball Club*, 468 F.2d 1064 (2d Cir. 1972).

We conclude that the evidence adduced by the Terminix companies does not establish that the parties contemplated substantial interstate activity when they entered the termite bond. Initially, we note that we have held in *A.J. Taft Coal Co. v. Randolph*, 602 So. 2d 395 (Ala. 1992)—which was decided under the *Costa & Head* standard—that it is insufficent for the purposes of invoking the FAA merely to show that one or more of the parties to the contract is located in another state. Therefore, under the more restrictive *Warren* standard, the fact that the bond stated that it was executed in Tennessee is not determinative. Terminix's second piece of evidence, that the bond stated that it was subject to federal regulation, is based on the following paragraph in the bond:

> "Change in Law. Terminix performs its services in accordance with the requirements of federal, state, and local law. In the event of a change in existing law as it pertains to the services promised herein, Terminix reserves the right to revise the annual extension charge or terminate this agreement."

A bare statement in the bond that Terminix adheres to the requirements of any federal law applicable to its services simply does not show that the parties contemplated that the bond would involve substantial interstate activity in any way. Unlike the contractual provisions in *Bennish, supra*, it certainly does not put the plaintiffs on notice of the likelihood of substantial interstate activity. Moreover, Gwin's statement that he wished to go with a "national" company is not evidence that he contemplated anything; that statement merely reflects a desire on Gwin's part to receive the added security that many people associate with a large, national company. Finally, the *performance* of the bond obligations did not involve interstate commerce to such a degree that the parties upon entering the contract must have contemplated substantial interstate activity. Although some materials used in fulfilling the bond obligations may have come from out-of-state suppliers, this is not analogous to those situations—such as the aforementioned construction contracts involving large projects, or contracts for personal services—where the interstate activity involved in the performance of the contract is so great that it cannot reasonably be said that the parties failed to contemplate substantial interstate activity when they entered into the contract. See *Terminix Int'l Co. v. Jackson*, [Ms. 1911842, Aug. 13, 1993] —— So. 2d —— (Ala. 1993).

For the foregoing reasons, the judgment of the trial court is due to be affirmed.

AFFIRMED.

Houston, Steagall, and Ingram, JJ., concur.

Kennedy, J., concurs in the result.

IN THE SUPREME COURT OF ALABAMA
SEPTEMBER 24, 1993

1920473

ALLIED-BRUCE TERMINIX COMPANIES, INC., *et al.*

v.

G. MICHAEL DOBSON, WANDA C. DOBSON, STEVEN GWIN, and JAN GWIN,

---

(Baldwin: CV-91-796)

NOTICE

The application for rehearing filed in this cause is overruled. No opinion written on rehearing.

ALMON J.—Houston, Steagall, Kennedy and Ingram, JJ., concur.

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MAY 19 1994
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No. 93-1001

In The Supreme Court of the United States

October Term, 1993

Allied-Bruce Terminix Companies, Inc., and Terminix International Company,
Petitioners,

v.

G. Michael Dobson, Wanda C. Dobson, Steven Gwin and Jan Gwin,
Respondents.

On Writ of Certiorari to the Supreme Court of Alabama

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QUESTION PRESENTED

Section 2 of the Federal Arbitration Act, 9 U.S.C. § 2, makes an agreement to arbitrate enforceable, as a matter of federal law, provided that it is part of "a contract evidencing a transaction involving commerce." The question presented here is whether Section 2 is inapplicable to contracts otherwise involving interstate commerce if the parties did not "contemplate[] substantial interstate activity" at the time of the contract.

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IN THE
Supreme Court of the United States
OCTOBER TERM, 1993

No. 93-1001

ALLIED-BRUCE TERMINIX COMPANIES, INC., and TERMINIX INTERNATIONAL COMPANY,
Petitioners,
v.
G. MICHAEL DOBSON, WANDA C. DOBSON, STEVEN GWIN and JAN GWIN,
Respondents.

On Writ of Certiorari to the Supreme Court of Alabama

BRIEF FOR PETITIONERS

OPINIONS BELOW

The opinion of the Supreme Court of Alabama is reported at 628 So. 2d 354. It is reprinted in the Joint Appendix at 97-103. The order of the circuit court is not reported. It is reprinted in the Joint Appendix at 96.

JURISDICTION

The judgment of the Supreme Court of Alabama was entered on August 13, 1993. A timely petition for rehearing was denied on September 24, 1993. The jurisdiction of this Court is invoked pursuant to 28 U.S.C. § 1257(3). This Court granted the petition for a writ of certiorari on March 21, 1994.

STATUTORY PROVISIONS INVOLVED

Section 2 of the Federal Arbitration Act, 9 U.S.C. § 2, provides:

> **Validity, irrevocability, and enforcement of agreements to arbitrate**
>
> A written provision in any maritime transaction or a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction, or the refusal to perform the whole or any part thereof, or an agreement in writing to submit to arbitration an existing controversy arising out of such a contract, transaction, or refusal, shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract.

Section 1 of the Federal Arbitration Act, 9 U.S.C. § 1, provides in relevant part:

> **"Maritime transactions" and "commerce" defined; exceptions to operation of title**
>
> . . . "commerce", as herein defined, means commerce among the several States or with foreign nations, or in any Territory of the United States or in the District of Columbia, or between any such Territory and another, or between any such Territory and any State or foreign nation, or between the District of Columbia and any State or Territory or foreign nation, but nothing herein contained shall apply to contracts of employment of seamen, railroad employees, or any other class of workers engaged in foreign or interstate commerce.

STATEMENT

This case involves the construction of Section 2 of the Federal Arbitration Act (the "FAA" or "the Act"), 9 U.S.C. § 2.[1] Section 2, as a matter of federal substantive

[1] All parties in the court below are reflected in the caption. The only corporate petitioner in this case—Allied-Bruce Terminix Cos., Inc.—has no parent company or subsidiaries.

law, requires enforcement of arbitration agreements in any "contract evidencing a transaction involving commerce." Section 1 of the Act defines commerce to include "commerce among the several States" (9 U.S.C. § 1). The Alabama Supreme Court refused to enforce the arbitration agreement in this case, however, on the ground that, notwithstanding any *actual* nexus with interstate commerce, the parties had not "*contemplated* substantial interstate activity." J.A. 100 (quoting *Metro Indus. Painting Corp. v. Terminal Constr. Co.*, 287 F.2d 382, 387 (2d Cir.), *cert. denied*, 368 U.S. 817 (1961) (Lumbard, J., concurring)).

The issue in this case arose out of an agreement between Steven and Jan Gwin and petitioners Allied-Bruce Terminix Companies, Inc. ("Terminix Service") and Terminix International Company ("Terminix International").[2] The Gwins, residents of Fairhope, Alabama, had previously agreed to a termite protection plan with a local company, but, upon its expiration, they decided "to go with a national company like Termin[i]x." J.A. 37. Terminix Service is an Arkansas company with offices in Florida, Georgia, Mississippi, Louisiana, Arkansas, Oklahoma, and Texas, as well as in Alabama. J.A. 71-72. Terminix International is a limited partnership with its principal place of business in Memphis, Tennessee. J.A. 79.

The termite protection plan provided for services to be performed by Terminix Service. Terminix International, in turn, guaranteed the terms of the plan. J.A. 80. The contract embodying the plan expressly provided that "any controversy or claim between [the parties] arising out of or relating to the interpretation, performance or breach of any provision of this agreement *shall be settled exclu-*

[2] As we discuss, the contract was later transferred to respondents Michael and Wanda Dobson pursuant to a contract for purchase of the Gwins' home. *See* page 4 *infra*.

sively by arbitration." J.A. 77-78, 79-80 (emphasis added).[3]

The termite protection plan was subsequently transferred to the Dobsons as part of their agreement to purchase the Gwins' home. J.A. 65-66.[4] In addition, Terminix Service performed a visual inspection of the home, as called for in the sales agreement, to check for active infestation. J.A. 38-39, 62-63. Both the termite protection plan and the written report on the visual inspection were presented to the Dobsons at the closing of the sale. J.A. 62-63, 69-70.

Shortly after the closing, in the course of remodeling the home, the Dobsons discovered termites. Petitioners then provided repairs and further treatment, in accordance with the terms of the termite protection plan. Much of the material and equipment used by petitioners to treat the home—specifically including the chemical used to

[3] The full text of the arbitration provision is as follows:

> The Purchaser and Terminix agree that any controversy or claim between them arising out of or relating to the interpretation, performance or breach of any provision of this agreement shall be settled exclusively by arbitration. Such arbitration shall be conducted in accordance with the Commercial Arbitration Rules then in force of the American Arbitration Association before three arbitrators appointed by the American Arbitration Association. The arbitration award shall be final and binding on both parties. Judgment upon such arbitration award may be entered in any court having jurisdiction.

J.A. 78.

[4] The sales agreement included the following provision:

> SELLER IS TO FURNISH WRITTEN EVIDENCE from a bonded and licensed termite control company that a visual inspection by them indicates the dwelling is free from infestation by wood destroying insects and damage caused by currently active infestation. OLD DAMAGE IS NOT CONSIDERED. The current termite contract, if any, is to be transferred to Buyer at Buyer's expense.

J.A. 66.

eliminate and prevent termites—was purchased outside of Alabama and brought into Alabama for use on the home. J.A. 71-72.

The Dobsons, however, remained dissatisfied. Rather than submit their complaints to arbitration, they elected to bring suit against petitioners in Alabama Circuit Court. After amendment of their original complaint, they ultimately asserted claims that petitioners had breached their duties under the termite protection plan, that they had negligently performed the visual inspection, and that they had misrepresented the results of the visual inspection.

Relying on the arbitration clause in the termite protection plan, petitioners sought to obtain a stay of the litigation and an order compelling arbitration. In so doing, petitioners specifically relied upon Section 2 of the Federal Arbitration Act. Petitioners argued that, as a matter of federal law, Section 2 required enforcement of voluntary arbitration agreements and that it preempted contrary state law. Without providing any reason, the Alabama Circuit Court, in a summary order, denied petitioners' motion. J.A. 96.

The Alabama Supreme Court, likewise, refused to enforce the written arbitration agreement. The court first noted that "[p]redispute arbitration agreements are unenforceable under Alabama law." J.A. 98 (citing Ala. Code 1975, § 8-1-41). The court acknowledged that Section 2 of the Federal Arbitration Act required enforcement of arbitration agreements as a matter of federal law, J.A. 98-99, but it held that Section 2 did not apply to this case because the required nexus with interstate commerce was absent. The court rejected petitioners' contention that the scope of Section 2—as reflected in the phrase "contract evidencing a transaction involving commerce"—should be broadly construed as "coextensive with [Congress'] commerce power." J.A. 99. Rather, the court opted to apply a more restrictive standard, stating that " '[t]he significant question, therefore [in determining

whether a contract evidences a transaction involving commerce] is not whether, in carrying out the terms of the contract, the parties *did* cross state lines, but whether, at the time they entered into it and accepted the arbitration clause, they *contemplated* substantial interstate activity.'" J.A. 100 (quoting *Metro Indus.*, 287 F.2d at 387 (Lumbard, J., concurring)).

Applying that test, the court determined that federal law did not apply. The court recognized that performance under the contract "involve[d] interstate commerce" but held that it did not do so "to such a degree that the parties upon entering the contract must have contemplated substantial interstate activity." J.A. 103. Pursuant to the state policy against enforcement of pre-dispute arbitration agreements, therefore, it declined to enforce the agreement.

SUMMARY OF ARGUMENT

Section 2 of the Federal Arbitration Act—enacted pursuant to the "comprehensive powers" of the Commerce Clause (*Southland Corp. v. Keating*, 465 U.S. 1, 15 (1984)—makes "valid, irrevocable, and enforceable" all written arbitration agreements in "a contract evidencing a transaction involving commerce . . . ." 9 U.S.C. § 2. Although this provision embodies "a liberal federal policy favoring arbitration agreements, notwithstanding any state substantive or procedural policies to the contrary," *Moses H. Cone Memorial Hosp. v. Mercury Constr. Co.*, 460 U.S. 1, 24 (1983), the Alabama Supreme Court gave it a narrow reading, holding that it applied only when the parties to a contract "*contemplated* substantial interstate activity." J.A. 100 (internal quotes omitted). This reading, however, is simply incorrect. Rather, as its language and policies demonstrate, "the Federal Arbitration Act . . . embodies Congress' intent to provide for the enforcement of arbitration agreements within the full reach of the Commerce Clause." *Perry v. Thomas*, 482 U.S. 483, 490 (1987).

1. The language of Section 2—the "primary substantive provision of the Act" (*Moses H. Cone*, 460 U.S. at 24)—indicates that Congress intended to exercise its commerce power broadly. Rather than limit the Act to transactions "in" commerce, Congress extended its reach to transactions "involving" commerce, a term that is properly used to mean "influenc[ing]" or "affect[ing]". *See The American Heritage Dictionary of the English Language* 950 (3d ed. 1992). Furthermore, the definition of "commerce," set forth in Section 1 of the Act (9 U.S.C. § 1), directly tracks the words used to define the commerce power ("commerce among the States") granted to Congress under Article I. And, while Section 2 provides that there must be a "contract evidencing" the transaction involving commerce, that language requires only that the contract be "evidence" of the transaction, not of the "commerce." The natural reading of Sections 1 and 2 of the Act, therefore, is that they mandate enforcement of arbitration agreements within the field over which Congress has constitutional power.

That reading of Section 2 is also most consistent with the "federal policy favoring arbitration." *Gilmer v. Interstate/Johnson Lane Corp.*, 111 S. Ct. 1647, 1652 (1991). This Court has often recognized that questions regarding the arbitrability of claims "must be addressed with a healthy regard for the federal policy favoring arbitration," *see Moses H. Cone*, 460 U.S. at 24, and the same regard should be applied to construction of the Act itself. Given its purpose of "ensur[ing] judicial enforcement of privately made agreements to arbitrate," *Dean Witter Reynolds, Inc. v. Byrd*, 470 U.S. 213, 219 (1985), it is highly unlikely that Congress would intentionally have left part of the field open for state policies hostile to arbitration agreements. *See Southland Corp.*, 465 U.S. at 14. And it is equally unlikely that Congress, in seeking to advance an alternative to litigation, would have defined the scope of the Act in a way that promotes ancillary litigation about the applicability of federal law and introduces fur-

ther uncertainty about the validity of private agreements to arbitrate.

Prior decisions of this Court, likewise, suggest that Congress, in enacting Section 2, exercised its commerce power fully. The statement in *Perry* to that effect (*see* page 6 *supra*) merely reflects earlier indications that Section 2 reaches "activity that affected commerce," *Bernhardt v. Polygraphic Co. of America*, 350 U.S. 198, 201 (1956), or "contracts relating to interstate commerce." *Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, 388 U.S. 395, 401 n.7 (1967) (quoting H.R. Rep. No. 96, 68th Cong., 1st Sess. 1 (1924)). The same broad interpretation of Section 2 is reflected in decisions of numerous federal courts of appeals. *See, e.g., Robert Lawrence Co. v. Devonshire Fabrics, Inc.*, 271 F.2d 402 (2d Cir. 1959), *cert. granted*, 362 U.S. 909, *cert. dismissed*, 364 U.S. 801 (1960); *Foster v. Turley*, 808 F.2d 38 (10th Cir. 1986); *Del E. Webb Constr. v. Richardson Hosp. Auth.*, 823 F.2d 145 (5th Cir. 1987).

2. Even if Section 2 were read to exercise less than the full commerce power, it could not be read to apply only when the parties to a contract "*contemplate* substantial interstate activity." That test, adopted from a concurring opinion by Judge Lumbard some thirty years ago, simply has no grounding in the Act. The language of the Act plainly calls for an objective, not a subjective, inquiry into the nature of the transaction—*i.e.*, whether it "involv[es] commerce"—and the opinion of Judge Lumbard gives no good reason for thinking otherwise. Thus, although the parties must subjectively agree *to arbitrate*, the scope of federal law does not further depend on what they contemplate about the interstate elements of the transaction.

The Alabama Supreme Court has stated that the "contemplation-of-the-parties" test "better promotes [its] strong public policy against the use of predispute arbitration agreements." *Lopez v. Home Buyers Warranty Corp.*, 628 So. 2d 361, 363 n.2 (Ala. 1993), *reh'g denied*, 1993

Ala. LEXIS 1512 (Sept. 24, 1993), *petition for cert. filed*, 62 U.S.L.W. 3430 (Dec. 22, 1993) (No. 93-995). But a hostility towards arbitration agreements is not a basis for giving a narrow reading to a federal law designed to displace that hostility. Of course, to the extent that the court below is concerned about the fairness of contracts containing arbitration agreements, Section 2, by its terms, allows for invalidation of agreements to arbitrate "upon such grounds as exist at law or in equity for the revocation of *any* contract." 9 U.S.C. § 2 (emphasis added); *see Gilmer*, 111 S. Ct. at 1655-56. What courts may not do, however, is to apply discriminatory state-law principles "that take[] [their] meaning precisely from the fact that a contract to arbitrate is at issue . . . ." *Perry*, 482 U.S. at 492 n.9. That is just what the court below has done here, and its action is invalid as a matter of federal law.

ARGUMENT

Section 2 of the Federal Arbitration Act "is a congressional declaration of a liberal federal policy favoring arbitration agreements, notwithstanding any state substantive or procedural policies to the contrary." *Moses H. Cone Memorial Hosp. v. Mercury Constr. Co.*, 460 U.S. 1, 24 (1983); *see Perry v. Thomas*, 482 U.S. 483, 489 (1987). Drawing upon its "comprehensive powers" under the Commerce Clause, *Southland Corp. v. Keating*, 465 U.S. 1, 15 (1984), Congress "create[d] a body of federal substantive law of arbitrability, applicable to any arbitration agreement within the coverage of the Act." *Moses H. Cone*, 460 U.S. at 24. Within the fields that it encompasses—"maritime transaction[s]" and "transaction[s] involving commerce"—Section 2 requires that courts "rigorously enforce agreements to arbitrate." *Dean Witter Reynolds, Inc. v. Byrd*, 470 U.S. 213, 221 (1985); *see Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 626 (1985). That obligation is binding on both federal and state courts. *See Southland Corp.*, 465 U.S. at 15.

The Alabama Supreme Court nevertheless held that it was free to deny enforcement of the arbitration agreement in this case, finding that federal law was inapplicable. The court reached this result by concluding that, whatever the actual nexus with interstate commerce, a transaction does not "involv[e] commerce" within the meaning of Section 2 unless "at the time they entered into [the contract] and accepted the arbitration clause, [the parties] *contemplated* substantial interstate activity." J.A. 100 (quoting *Metro Indus. Painting Corp. v. Terminal Constr. Co.*, 287 F.2d 382, 387 (2d Cir.), *cert. denied*, 368 U.S. 817 (1961) (Lumbard, J., concurring) (*Metro Indus.*). Thus, even though the parties here had agreed to arbitrate all disputes arising out of the transaction, and even though the transaction involved parties in different states and materials shipped across state lines, the federal policy favoring enforcement of arbitration agreements was disregarded. In its place, the court applied state law *barring* enforcement of predispute arbitration agreements.

This reading of Section 2 is simply indefensible. To arrive at it, the court below necessarily accepted two propositions with respect to congressional intent: first, that Congress, in exercising its power over interstate commerce, meant to use only a fraction of that power and, second, that, in doing so, Congress further intended to make the parties' subjective views *about the extent of interstate commerce* into the touchstone of Section 2 application. Both propositions are incorrect. The language and policies of the Act demonstrate that Congress wanted to override legislative and judicial hostility to arbitration agreements to the full extent of its powers and that, in any event, it is the actual nexus of transactions to interstate commerce, not the subjective views of the contracting parties, that defines the jurisdictional reach of Section 2.

I. SECTION 2 APPLIES TO WRITTEN ARBITRATION AGREEMENTS TO THE FULL EXTENT OF LEGISLATIVE POWER UNDER THE COMMERCE CLAUSE

The purpose of the Federal Arbitration Act, originally enacted in 1925, was "to ensure judicial enforcement of privately made agreements to arbitrate." *Dean Witter Reynolds*, 470 U.S. at 219; *see Gilmer v. Interstate/Johnson Lane Corp.*, 111 S. Ct. 1647, 1651 (1991); *Scherk v. Alberto-Culver Co.*, 417 U.S. 506, 510 n.4 (1974). As this Court has stated, "[t]he problems Congress faced were . . . twofold: the old common-law hostility toward arbitration, and the failure of state arbitration statutes to mandate enforcement of arbitration agreements." *Southland Corp.*, 465 U.S. at 14. The Act sought "to place an arbitration agreement 'upon the same footing as other contracts, where it belongs.'" *Dean Witter Reynolds*, 470 U.S. at 219 (quoting H.R. Rep. No. 96, 68th Cong., 1st Sess. 1 (1924)).

The "primary substantive provision of the Act" (*Moses H. Cone*, 460 U.S. at 24) is Section 2, which provides that arbitration agreements "shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract." To be within the scope of the Act, however, an arbitration provision must meet two conditions: first, it must be written and, second, it must be "in any maritime transaction or a contract evidencing a transaction involving commerce." Section 1 of the Act defines the term "commerce" to "mean[] commerce among the several States or with foreign nations . . . ."

The reference to "transactions involving commerce" in Section 2 indicates what this Court has repeatedly recognized: that, in enacting Section 2, Congress was relying upon its powers under the Commerce Clause. *See Perry*, 482 U.S. at 491 & n.8; *Southland Corp.*, 465 U.S. at 14-15; *Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, 388

U.S. 395, 405 (1967). That much was settled (after some debate) by the decision in *Prima Paint*, where the Court expressly held that "the federal arbitration statute is based upon and confined to the incontestable federal foundations of 'control over interstate commerce and over admiralty.'" 388 U.S. at 405 (quoting H.R. Rep. No. 96, 68th Cong., 1st Sess. 1 (1924)); S. Rep. No. 536, 68th Cong., 1st Sess. 3 (1924). Later, in holding that Section 2 of the Act applies in state as well as federal courts, the Court emphasized the fact that Congress had "draw[n] on the comprehensive powers of the Commerce Clause." *Southland Corp.*, 465 U.S. at 15.

Given the breadth of these "comprehensive powers," there seems little doubt that, so long as Congress exercised them to the fullest, the arbitration agreement in this case is enforceable as a matter of federal law. One hundred years before passage of the Act, this Court stated that the federal power over interstate commerce is "complete in itself, may be exercised to its utmost extent, and acknowledges no limitations other than are prescribed in the constitution." *Gibbons v. Ogden*, 22 U.S. (9 Wheat.) 1, 196 (1824); *see also Hodel v. Virginia Surface Mining & Reclamation Ass'n*, 452 U.S. 264, 276 (1981) ("the Commerce Clause is a grant of plenary authority to Congress."). And, it is now accepted that the power over commerce "extends not only to 'the use of channels of interstate or foreign commerce' and to 'protection of the instrumentalities of interstate commerce . . . or persons or things in commerce,' but also to 'activities affecting commerce.'" 452 U.S. at 276-77 (quoting *Perez v. United States*, 402 U.S. 146, 150 (1971)).[5] Thus, "[e]ven

[5] Although the boundaries of the Commerce Clause have been subject to varying definitions over the years, decisions prior to passage of the Act had indicated that its scope extended at least to contracts "concerning interstate commerce" (*American Express Co. v. Iowa*, 196 U.S. 133, 143 (1905)) or to intrastate activities "burden[ing]" interstate commerce. *Board of Trade v. Olsen*, 262 U.S. 1, 36 (1923). *See also Stafford v. Wallace*, 258 U.S. 495, 521 (1922). Indeed, a brief submitted to Congress in 1924, by Julius H. Cohen, a member of the Committee on Commerce, Trade & Commercial Law of the ABA and General Counsel for the N.Y. State Chamber of Commerce, stated that "[i]t is not only the actual and physical interstate shipment of goods which is subject to the interstate commerce powers of the Federal Government, but these powers govern every agency or act which bears so close a relationship to interstate commerce that they can reasonably be said to affect it. Contracts relating to interstate commerce are within the regulatory powers of Congress. (*Board of Trade v. Olsen*, U.S.S.C. Adv. Op. No. 13, May 1, 1923, p. 519; *American Express Co. v. Iowa*, 196 U.S. 133, 143.)" Joint Hearings on S. 1005 & H.R. 646 Before the Subcomm. of the Comms. on the Judiciary, 68th Cong., 1st Sess. 38 (1924). The House Report subsequently used the same language ("contracts relating to interstate commerce") in describing the scope of the powers granted by the Commerce Clause. *See* page 14 *infra*.

activity that is purely intrastate in character may be regulated by Congress, where the activity, combined with like conduct by others similarly situated, affects commerce among the States or with foreign nations." *Fry v. United States*, 421 U.S. 542, 547 (1975); *Wickard v. Filburn*, 317 U.S. 111, 127-28 (1942). The "activity" here—written agreements between parties of different States for the provision of continuing services that involve materials from other States—readily meets that test.

A. The issue before this Court arises, therefore, only because the Alabama Supreme Court held that Congress did *not* utilize the full extent of its power under the Commerce Clause, thus leaving room for state policies hostile to arbitration within the field. But neither the court below, nor any other court, is able to support that view by reference to the language—or the policies (*see* pages 17-20 *infra*)—of the Act. To the contrary, the language points in just the opposite direction. The field to which Section 2 applies is marked out as any "transaction involving commerce," and Section 1 defines "commerce" to mean "commerce among the several States." The words of that definition, of course, are exactly the same as the words used to define the power given to Congress under Article

I: "to regulate commerce among the several States." Thus, in the absence of other language compelling a narrower construction, the most natural reading of Sections 1 and 2, taken together, is that Section 2 applies throughout the field ("commerce among the several States") over which Congress has power under Article I.

The remainder of Section 2, however, is bereft of any narrowing language. In particular, although Congress could have defined the coverage of the Act by reference to transactions "in" commerce, it chose not to do so, but extended the Act to transactions "involving" commerce. That term, on its face, is broader and more inclusive. *See, e.g., United States v. Luskey*, 262 U.S. 62 (1923); *United States v. James*, 834 F.2d 92, 93 (4th Cir. 1987); *Board of Trade v. SEC*, 677 F.2d 1137, 1146-48 & n.17 (7th Cir.), *vacated as moot*, 459 U.S. 1026 (1982). Indeed, as a matter of common usage, the word "involving" is readily employed to indicate that one matter (here, the transaction) has an effect on, or is related to, a second matter (here, interstate commerce). *See The American Heritage Dictionary of the English Language* 950 (3d ed. 1992) (defining "involve" to mean, *inter alia*, "[t]o influence or affect"). Transactions that affect, or relate to, commerce are within the constitutional power of Congress to regulate. *See* pages 12-13 *supra*.

This understanding of the word "involving" is, in turn, reflected in the discussion of Section 2 in the relevant House Report, on which this Court has previously relied in construing the Act. *See Prima Paint*, 388 U.S. at 401 n.7 (discussed *infra* at page 21). That Report first noted that the remedy provided for in Section 2 is "founded . . . upon the Federal control over interstate commerce." Having established that basis for the Act, it then specifically declared that "[t]he control over interstate commerce reaches not only the actual physical interstate shipment of goods but also *contracts relating to interstate commerce*." H.R. Rep. No. 96 at 1 (emphasis added). *See also* 65 Cong. Rec. 1931 (1924) (Statement

of Rep. Graham) (Act "only affects contracts relating to interstate subjects and contracts in admiralty").[6] And, this Court has made use of the word "involving" to describe the extent of congressional power under the Commerce Clause, pointing out that Congress enacted Section 2 on the basis of that power and observing that the "reach [of the Commerce Clause] would be limited to transactions involving interstate commerce." *Southland Corp.*, 465 U.S. at 14.

The only other words potentially limiting the scope of Section 2 are the words "contract evidencing," which precede the phrase "a transaction involving commerce." But those words, likewise, reveal no intent to exercise the commerce power sparingly. Taken at face value, the language says nothing more than that the contract must be evidence of the *transaction*, not of the "commerce" to which it applies. Thus, so long as the transaction actually "involv[es]" interstate commerce, and so long as the contract "evidenc[es]" the transaction, Section 2 makes the agreement to arbitrate enforceable regardless of whether the parties openly make reference to the interstate elements in their contract.

If there were any question about this reading, a review of the history of the phrase "contract evidencing" confirms that it was not meant to pare back exercise of the commerce power. The phrase was absent from the earlier version of the bill, which applied broadly to "a written provision in any contract or maritime transaction or transaction involving commerce." S. 4214, 67th Cong., 4th Sess. (1922); S. 1005, 68th Cong., 1st Sess. (1923);

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[6] Congress has used the term "affecting commerce" as a way of declaring its intent to exercise its full commerce power, *see Gulf Oil Corp. v. Copp Paving*, 419 U.S. 186 (1974), and the term "involving commerce" is sufficiently close in meaning to signal the same intent. Had Congress wished to indicate that it was invoking less than all of its power, in fact, it is natural to suppose that it would have used the term "in" instead. *See id.* at 194-95.

H.R. 646, 68th Cong., 1st Sess. (1924).[7] That language ("any contract"), if read literally, would have made *all* arbitration provisions enforceable, and, as a consequence, raised the most serious questions about the source of congressional authority. The changed language effectively avoided those questions, confining the statute to those fields within Congress' acknowledged control.[8] *See Southland Corp.*, 465 U.S. at 14-15 (describing the "involving commerce" requirement as a "*necessary* qualification on a statute intended to apply in state and federal courts") (emphasis added). But, while Congress did what was necessary to stay within its allotted powers, there is no reason to think that Congress—legislating with the extent of its own powers in mind—went even further and left some (undefined) portion of its power unexercised.[9] Rather, Congress appears to have done just what the language of the Act suggests: tailored the scope of the Act to the scope of its power under the Commerce Clause, no more and no less.

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[7] The language of Section 2 was modeled after a New York law, which provided that "[a] provision in a written contract to settle by arbitration a controversy thereafter arising between the parties to the contract . . . shall be valid, enforcible [sic] and irrevocable, save upon such grounds as exist at law or equity for the revocation of any contract." Act of April 19, 1920, ch. 275, 1920 N.Y. Laws 803.

[8] The Fourth Circuit has thus surmised that "[t]his was evidently done because it was realized that Congress had no power to legislate with respect to the validity of contracts generally but only as to the validity of those which related to matters subject to its control." *Agostini Bros. Bldg. Corp. v. United States*, 142 F.2d 854, 856 (4th Cir. 1944).

[9] We note that Congress did not change the introductory language of the bill, which states that the bill is "[t]o make valid and enforceable written provisions or agreements for arbitration of disputes arising out of contracts, maritime transactions, or commerce among the States or Territories or with foreign nations." Pub. L. No. 68-401, 43 Stat. 883 (1925). If that language were given effect with regard to Section 2, of course, it would only serve to extend the coverage of the Act beyond the scope of the maritime and commerce powers, not restrict it to something less.

B. This reading of Section 2 also fits closely with the policies embodied in the Act as a whole. It is well-established that, "[i]n enacting § 2 of the federal Act, Congress declared a national policy favoring arbitration and withdrew the power of the states to require a judicial forum for the resolution of claims which the contracting parties agreed to resolve by arbitration." *Southland Corp.*, 465 U.S. at 10; *Perry*, 482 U.S. at 489. This Court has emphasized that, in deciding whether particular federal statutory claims are appropriate for arbitration, " 'questions of arbitrability must be addressed with a healthy regard for the federal policy favoring arbitration.' " *Gilmer*, 111 S. Ct. at 1652 (quoting *Moses H. Cone*, 460 U.S. at 24).[10] And it has declared that this "healthy regard" for federal policy must be taken into account in resolving other issues involving arbitration as well: "[t]he Arbitration Act establishes that, as a matter of federal law, *any doubts concerning the scope of arbitrable issues should be resolved in favor of arbitration*, whether the problem at hand is the construction of the contract language itself or an allegation of waiver, delay, or a like defense to arbitrability." *Moses H. Cone*, 460 U.S. at 24-25 (emphasis added).

These same principles should naturally be applied to construction of the Act itself. Just as the "federal policy favoring arbitration" places a special burden on litigants challenging arbitration of claims under federal statutes—requiring them to show that the federal policy is somehow inapplicable to those claims (*see, e.g., Gilmer*, 111 S. Ct. at 1652; *Shearson/American Express, Inc. v. McMahon*, 482 U.S. 220, 227 (1987))—it should place a similar burden on litigants seeking to avoid arbitration of disputes within the reach of Congress' power under the Commerce

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[10] As the Court stated in *Gilmer*, "[h]aving made the bargain to arbitrate, the party should be held to it unless Congress itself has evinced an intention to preclude a waiver of judicial remedies for the statutory rights at issue." 111 S. Ct. at 1652 (quoting *Mitsubishi Motors*, 473 U.S. at 628).

Clause. In the one case as the other, it is reasonable to presume that, absent other indications, Congress fully intended for its policy to apply. Although this presumption naturally would yield to contrary plain language, there is, as we have discussed, no language in the Act indicating an intent to dispense with federal policy. To the contrary, this Court has observed (with respect to arbitration of statutory claims) that "the [Federal Arbitration] Act itself provides no basis for disfavoring agreements to arbitrate statutory claims by skewing the otherwise hospitable inquiry into arbitrability." *Mitsubishi Motors,* 473 U.S. at 627. By the same token, the Act gives no basis for thinking that Congress meant to limit its application to some indeterminate portion of transactions over which it has constitutional power.

It is difficult, in fact, to imagine any reason why Congress would deliberately base this legislation upon its broad power over commerce and yet exercise only a fraction of that power. There can be no serious concern that the Arbitration Act would so expand federal law as to inundate the federal courts with burdensome litigation: the Act does not itself provide a basis for jurisdiction in the federal courts (*see Moses H. Cone,* 460 U.S. at 25 n.32) and, in any event, the Act contains only a few, clear commands designed to *reduce* litigation by removing the substance of disputes from the courts. Nor is there evidence that Congress affirmatively recognized and wished to defer in some measure to state policies directly contrary to the Act's policy favoring fulfillment of promises to arbitrate. Accordingly, to decide that Congress used only part of its power, this Court would ultimately have to conclude that, regardless of the effect on commerce, Congress intentionally left room for contracting parties to disavow agreements to arbitrate and for States to apply discriminatory laws hostile to arbitration. But that conclusion would run head on into the basic purpose of the Act: to assure that arbitration agreements are given

the same respect as all other contracts. Whereas Congress was unquestionably willing for States to apply *neutral* laws to arbitration agreements—at least with respect to certain issues—it plainly was not willing to have States apply *discriminatory* laws to those agreements.

It is also highly doubtful that Congress would have defined the field in a manner that promotes ancillary litigation about the enforceability of arbitration agreements The Act was passed against a background of "agitation against the costliness and delays of litigation," *Dean Witter Reynolds,* 470 U.S. at 220 (quoting H.R. Rep. No. 96 at 2), and Congress expected that "[t]hese matters can be largely eliminated by agreements for arbitration, if arbitration agreements are made valid and enforceable." *Id.* The benefits of arbitration would be substantially diminished, however, if disputes over the nexus with interstate commerce (or, even worse, over the parties' "contemplation" of interstate commerce) had to be resolved to determine whether agreements to arbitrate are binding in the first place. Although some litigation is presumably unavoidable under any standard, it seems safe to say that litigation will be the least pervasive with respect to whether the contract falls within the field that Congress has power to regulate under the Commerce Clause. Written agreements involving the sale of goods and services will typically be within that field.

A reduction in the number of ancillary disputes will also promote the goal of certainty in commercial dealings. Under federal law, businesses engaged in a transaction involving interstate commerce should be able to rely on an agreement to arbitrate disputes between the contracting parties.[11] But if courts must examine the facts of each

[11] One witness testified that the provisions of the bill sought, among other things, "to reduce the price of commodities to the consumer; . . . on the theory that a merchant in figuring his cost adds to his price a certain amount representing the risk of rejection, claims, fault-finding, etc., even including litigation. If inexpensive but dependable arbitration were possible instead of

transaction to determine whether it fits within some constricted definition of "involving commerce," it frequently will be difficult for businesses to know, at the time that they negotiate contracts, whether agreements to arbitrate are binding or not. Whatever the outcome of litigation over this question, the uncertainty itself is inconsistent with Congress' goal of making arbitration agreements valid and enforceable as a matter of federal law. 9 U.S.C. § 2.

C. Prior decisions of this Court also suggest that Section 2 was intended to have broad reach. The most recent, and clearest, statement of that view was contained in *Perry*, where the Court held that the Act preempted state law barring arbitration of designated claims. *See* 482 U.S. at 491. There, the Court first distinguished provisions of the 1934 Securities Act and related regulations—which it previously had held not to preempt the same state law (*See Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Ware*, 414 U.S. 117 (1973))—on the ground that nothing in those materials had "specifie[d] arbitration as the favored means of resolving employer-employee disputes." 482 U.S. at 490 (quoting *Ware*, 414 U.S. at 135). The Court then went on to state that the preemptive effect of the Federal Arbitration Act was far more extensive, expressly describing it as "a statute that embodies Congress' intent to provide for the enforcement of arbitration agreements *within the full reach of the Commerce Clause.*" *Id.* (emphasis added).

This language reflects an understanding contained in earlier cases as well. Thus, although the Court, in *Bernhardt v. Polygraphic Co. of America*, 350 U.S. 198

costly, time-consuming, and troublesome litigation, the risk would be correspondingly smaller and the price made to conform therewith." Hearing on S. 4213 and S. 4214 Before a Subcomm. of the Comm. on the Judiciary, 67th Cong., 4th Sess. 3 (1923) (Statement of Charles L. Bernheimer, Chairman of the Arbitration Comm. of the N.Y. State Chamber of Commerce).

(1956), held that a particular employment contract did not evidence a transaction involving commerce, it applied a test that reflects the full extent of Congress' power over interstate commerce: it thus declined to apply the Act only after finding "no showing that [the employee] while performing his duties under the employment contract was working 'in' commerce, was producing goods for commerce, or was engaging in *activity that affected commerce*, within the meaning of our decisions." *Id.* at 200-01 (emphasis added).[12] Similarly, a decade later, in *Prima Paint Corp.*, 388 U.S. 395, the Court expressly rejected an argument that Congress had intended Section 2 to apply narrowly only to "contracts between merchants for the interstate shipment of goods," *id.* at 401 n.7, finding no basis for that reading in either the language or history of the Act. The Court found specific support for broader application of the Act in language from the House Report, noted earlier at pages 14-15, which stated that the commerce power exercised by Congress extended to " '*contracts relating to interstate commerce.*' " *Id.* (quoting H.R. Rep. No. 96 at 1 (emphasis added).

The federal courts of appeals, to the extent that they have addressed the issue, have also given the Act broad sweep. *See, e.g., Snyder v. Smith*, 736 F.2d 409, 417-18 (7th Cir.), *cert. denied*, 469 U.S. 1037 (1984); *Societe Generale de Surveillance, S.A. v. Raytheon European Management & Sys. Co.*, 643 F.2d 863, 867 (1st Cir. 1981); *Foster v. Turley*, 808 F.2d 38 (10th Cir. 1986); *Del E. Webb Constr. v. Richardson Hosp. Auth.*, 823 F.2d

[12] By holding that the employment agreement in *Bernhardt* did not "involve commerce"—a somewhat surprising conclusion, given the test that the Court applied—the Court was able to put aside the constitutional question whether, after *Erie R. Co. v. Tompkins*, 304 U.S. 64 (1938), Congress could prescribe substantive rules of decision for diversity cases in federal court. This Court disposed of that question in *Prima Paint*, holding that Congress could do so by exercising its powers over interstate commerce and admiralty. 388 U.S. at 405.

145, 147 (5th Cir. 1987). *See also Woermann Constr. Co. v. Southwestern Bell Tel. Co.*, 846 S.W.2d 790, 792 (Mo. Ct. App. 1993). In a leading decision more than 30 years ago, the Second Circuit—having recounted the history of judicial hostility toward enforcement of arbitration agreements—reasoned that "the Congress took pains to utilize as much of its power as it could and by doing so it sought to reduce to a minimum the danger of judicial rejection on constitutional grounds." *Robert Lawrence Co. v. Devonshire Fabrics, Inc.*, 271 F.2d 402, 407 (2d Cir. 1959), *cert. granted*, 362 U.S. 909, *cert. dismissed*, 364 U.S. 801 (1960). More recently, the Tenth Circuit, noting the federal policy favoring arbitration, concluded that "[t]he requirement that the underlying transaction involve commerce is to be broadly construed *so as to be coextensive with congressional power to regulate under the Commerce Clause.*" *Foster v. Turley*, 808 F.2d at 40 (emphasis added). Similarly, the Fifth Circuit has held that Section 2 applies to any contracts that "*relate* to interstate commerce, a standard that implements the strong federal policy favoring arbitration." *Del E. Webb Constr. v. Richardson Hosp. Auth.*, 823 F.2d at 148. And the First Circuit has declared that "the term 'commerce' in this provision of the Act refers to interstate or foreign commerce and is to be broadly construed." *Societe Generale*, 643 F.2d at 867. *See also Mesa Operating Ltd. Partnership v. Louisiana Intrastate Gas Corp.*, 797 F.2d 238, 243 (5th Cir. 1986) ("Commerce" under the Act includes all contracts relating to interstate commerce); *American Airlines, Inc. v. Louisville and Jefferson County Air Bd.*, 269 F.2d 811 (6th Cir. 1959) (Act was enacted pursuant to Congress' plenary power over interstate commerce); *First Investors Corp. v. American Capital Financial Servs., Inc.*, 823 F.2d 307 (9th Cir. 1987) (Act governs agreements "affecting" interstate commerce).

These decisions, at bottom, all recognize what is apparent from the Act itself: that Congress wanted to make

arbitration agreements enforceable across a broad spectrum of commercial arrangements. The Act does not mandate that parties enter into an agreement to arbitrate their disputes. But, once they have done so, and have done so with respect to a transaction within Congress' power to regulate, then that agreement is to be enforced—to the same extent as any other agreement—as a matter of federal law.

II. SECTION 2 CANNOT BE READ, IN ANY EVENT, TO REQUIRE THAT THE PARTIES CONTEMPLATE SUBSTANTIAL INTERSTATE ACTIVITY

Even if Section 2 were read to exercise less than all of the power granted to Congress under the Commerce Clause, it could not reasonably be read to apply only to situations in which, at the time that the parties entered into the agreement to arbitrate, they "contemplated substantial interstate activity." That test—turning on the parties' state of mind with respect to interstate commerce—finds no basis whatsoever in the Act.

The subjective test, first announced by Judge Lumbard in a concurring opinion some thirty years ago, provides that the decisive inquiry for courts applying Section 2 is simply "whether, at the time [the parties] entered into [the contract] and accepted the arbitration clause, they *contemplated* substantial interstate activity." *Metro Indus.*, 287 F.2d at 387. The various courts following the Lumbard test thus make the scope of federal law turn "not on what in fact happened, but on what was in the contemplation of the parties as manifested in their written agreement." *Id. See, e.g., Burke County Pub. School Bd. of Educ. v. Shaver Partnership*, 279 S.E.2d 816 (N.C. 1981); *Pathman Constr. Co. v. Knox County Hosp. Ass'n*, 326 N.E.2d 844 (Ind. Ct. App. 1975); *R.J. Palmer Constr. Co. v. Wichita Band Instrument Co.*, 642 P.2d 127 (Kan. Ct. App. 1982); *Loche v. Dean Witter Reynolds, Inc.*, 526 N.E.2d 1296 (Mass. App. Ct. 1988); *Lacheney v. Profitkey Int'l, Inc.*, 818 F. Supp. 922 (E.D. Va. 1993). As

might be expected, the application of this test frequently has the effect of diminishing the reach of federal law: in this case, for example, the Alabama Supreme Court did not question that the transaction *in fact* involved interstate activity, but it found the activity insufficient to support an inference that the parties contemplated it at the time of the contract. It thus felt free to apply state, not federal, law.

This view simply cannot be squared with the terms of the Act. The term "transaction involving commerce" calls for an inquiry into the transaction itself, not the expectations of the parties, and the broad definition of "commerce" in Section 1 ("commerce among the several States") provides a wholly objective standard for that inquiry. And, as we have noted (*see* page 15 *supra*), the requirement that the contract "evidenc[e]" the transaction involving commerce—added to prevent application of the Act beyond the extent of Congress' powers—means only that the contract must be evidence of the transaction, not that it reflect the particular interstate elements. Indeed, it would be almost inexplicable for Congress to have wanted the jurisdiction of the Act to depend in every case upon what the parties' *subjectively* understood about the extent of interstate commerce involved.[13]

The opinion of Judge Lumbard, likewise, provides no basis for thinking that Congress had a subjective test in mind. Indeed, while Judge Lumbard discussed the language and history of the Act at some length, he ultimately pulled the "contemplation-of-the-parties" test more or less out of thin air. The bulk of his opinion, in fact, is devoted to establishing a proposition that is, in the main,

[13] It is well accepted, for example, that defendants need not be aware of the jurisdictional elements contained in federal criminal statutes. *See United States v. Yermian*, 468 U.S. 63, 68-69 (1984) (quoting *United States v. Feola*, 420 U.S. 671, 676-77 (1975) ("the existence of the fact that confers federal jurisdiction need not be one in the mind of the actor at the time he perpetrates the act made criminal by the federal statute")).

unobjectionable: that "the purpose of the act was to assure those who desired arbitration and whose contracts *related to interstate commerce* that their expectations would not be undermined by federal judges, or . . . by state courts or legislatures." 287 F.2d at 387 (emphasis added). But, having reached that conclusion, Judge Lumbard announced, in the very next sentence, that the "significant question, therefore," was whether the parties "*contemplated* substantial interstate activity." The word "therefore" notwithstanding, however, the conclusion does not properly follow from the premise.[14] If the parties "desire[] arbitration," and the transaction provided for in their contract in fact "relate[s] to interstate commerce," then nothing more is needed to bring their agreement within the boundaries of the Act, regardless of what they do or do not contemplate about the interstate elements.[15]

The "contemplation-of-the-parties" test, in the end, mixes together two necessary, but ultimately distinct, elements under Section 2: first, an agreement to arbitrate; and, second, a nexus to interstate commerce. The first element requires a subjective inquiry into the "contemplation" of the parties to determine whether a necessary precondition of Section 2 has been met: that is, whether the

[14] Not only does the reference to the parties' "contemplat[ion]" appear from nowhere, but the reference to "substantial" interstate activity does as well. The vagueness of that term—and the prospect of litigation over its application in individual cases—is further reason for doubting that Congress intended to tie enforceability of arbitration agreements to this sort of inquiry.

[15] There is no reason to believe that parties to a contract openly agree to arbitration agreements, while secretly believing that the contract does not involve interstate commerce and that the agreement is thus unenforceable under state law. Nor is there reason to believe that, in a transaction actually involving interstate commerce, Congress would want that strategy to be rewarded. Unless that unexpressed belief would be grounds for avoiding the obligations by any contract, it is not grounds for refusing to comply with an agreement to arbitrate. *See* page 27 *infra*.

parties have entered into a voluntary agreement to arbitrate their disputes. The second element calls for an objective inquiry to determine whether the transaction is within the field over which Congress has legislated and within reach of the powers allotted to Congress under the Constitution. But it completely distorts the Act to combine these independent requirements (one subjective and one objective) into a third (mixed) requirement: that the parties must subjectively "contemplate" the objective elements necessary to bring the transaction within the terms of the statute and the Constitution. Once it has been determined that the parties have agreed to arbitrate their disputes, the inquiry into their intent is properly at an end; the sole remaining inquiry is whether Congress, having exercised its power over interstate commerce, has made that agreement enforceable.[16]

To explain its adoption of the "contemplation-of-the-parties" test, the Alabama Supreme Court has stated openly that the test "better promotes [its] strong public policy against the use of predispute arbitration agreements." *Lopez v. Home Buyers Warranty Corp.*, 628 So.2d 361, 363 n.2 (Ala. 1993), *reh'g denied*, 1993 Ala. LEXIS 1512 (Sept. 24, 1993), *petition for cert. filed*, 62 U.S.L.W. 3430 (Dec. 22, 1993) (No. 93-995).[17] But, to state the

[16] Given that contracts (like the one in this case) are often transferred to other parties, the test would also be extraordinarily difficult to apply. A party assuming a contract from persons meeting the subjective test—*i.e.*, persons who did contemplate the interstate activities—should not be able to avoid arbitration by arguing that he did not have the same state of mind. But it would be highly inconvenient, at best, to inquire into the understanding of the original parties, wherever they may be, before it can be determined whether the arbitration agreement (voluntarily assumed as part of the contract) can be enforced.

[17] The Alabama Supreme Court has recently relied on that same "public policy" in deciding arbitration issues, even with respect to agreements that are concededly within the scope of Section 2. *See Old Republic Ins. Co. v. Lanier*, No. 1921387, 1994 Ala. LEXIS 276 (Ala. Apr. 29, 1994).

obvious, a distrust of arbitration is hardly a good reason to read Section 2 narrowly. As this Court has observed, "we are well past the time when judicial suspicion of the desirability of arbitration and of the competence of arbitral tribunals inhibited the development of arbitration as a means of dispute resolution." *Mitsubishi Motors*, 473 U.S. at 626-27. The Alabama courts and legislature may believe that arbitration agreements are undesirable; but the Act reflects *Congress'* contrary belief that arbitration provides a fair and efficient remedy to persons engaged in contractual disputes. *See id.* at 628 (parties agreeing to arbitrate do not forfeit substantive rights; they only "submit[] to their resolution in an arbitral, rather than a judicial, forum"). And it is clear that, for contracts within the terms of the Act, Congress intended its view of arbitration to prevail.

The federal policy favoring arbitration does not mean, of course, that every arbitration agreement involving interstate commerce is valid and binding. This Court has recognized that agreements to arbitrate may "result[] from the sort of fraud or overwhelming economic power that would prove grounds 'for the revocation of any contract.'" *Mitsubishi Motors*, 473 U.S. at 627 (quoting 9 U.S.C. § 2); *see Gilmer*, 111 S. Ct. at 1655-56. If that is the case, the agreement need not be enforced. But, as the language of Section 2 makes clear, the grounds on which States may refuse to enforce arbitration agreements must be grounds that apply to other contracts as well: "Thus state law, whether of legislative or judicial origin, is applicable *if* that law arose to govern issues concerning the validity, revocability, and enforceability of contracts generally." *Perry*, 482 U.S. at 492 n.9. On the other hand, "[a] state-law principle that takes its meaning precisely from the fact that a contract to arbitrate is at issue does not comport with this requirement of § 2." *Id.*

The Alabama law involved here—a law expressly barring enforcement of predispute arbitration agreements—is the most notorious possible example of a state-law prin-

ciple that applies to arbitration agreements alone. To avoid preemption of that state law, therefore, the Alabama courts had no choice but to adopt a reading of Section 2 that made federal law wholly inapplicable. But a State may not shelter laws hostile to arbitration by turning that same hostility towards construction of federal arbitration law. Here, parties in different states entered into a contract for a continuing service, and that service involved materials brought from one state to another. By any reasonable standard, those dealings are a "transaction involving commerce," and the parties' agreement to arbitrate disputes arising out of that transaction must be enforced as a matter of federal law.

CONCLUSION

The judgment of the Supreme Court of Alabama should be reversed.

Respectfully submitted,

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May 19, 1994

BEST AVAILABLE COPY

QUESTIONS PRESENTED

The Federal Arbitration Act of 1925 provides for the enforceability in certain circumstances of arbitration agreements contained in "*a contract evidencing a transaction involving commerce*." 9 U.S.C. § 2. The state court below and numerous other courts construe the Act to apply only where the parties contemplate, at the time of contracting, engaging in substantial interstate activity in carrying out the terms of the contract — so that the contract *itself* "evidenc[es]" an interstate commercial transaction. Three questions are presented here:

1. Should this Court overrule its holding that the Federal Arbitration Act governs proceedings in state courts — a holding announced without the benefit of briefing and without notice to the States, in *Southland Corporation v. Keating*, 465 U.S. 1, 12-16 (1984)?

2. Does § 2's "contract evidencing" language require a court to determine whether the terms of the contract, as well as other objective indicia of its meaning, show that in making the contract the parties contemplated engaging in "a transaction involving commerce"?

3. Does § 2's "transaction involving commerce" language require a court to determine whether the transaction at issue is actually a part of the "current" or "flow" of interstate commerce?

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BRIEF OF RESPONDENT

STATEMENT OF THE CASE

This case involves application of the Federal Arbitration Act (the "FAA" or "the Act"), 9 U.S.C. §§ 1 et seq., to a lawsuit in the Alabama state courts arising from termite inspection and extermination services provided to Alabama homeowners by service personnel who are trained, licensed, based and supervised entirely in Alabama.

1. The Contract.

The contract in question, a "Termite Protection Plan," J.A. 75,[1] or "termite bond," Pet. App. 1a; Rec. 1579, was entered into by respondents herein, G. Michael Dobson and Wanda C. Dobson, on May 10, 1991. On that date, the Dobsons purchased a home in Fairhope, Alabama, from respondents Steven and Jan Gwin.[2] At the closing, the Gwins assigned over to the Dobsons their existing termite bond, as they had earlier agreed upon, J.A. 66 ¶ 16, and as expressly authorized by the termite bond itself.[3]

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[1] Citations to the Joint Appendix will be styled "J.A. ___." Citations to the Appendix to the Petition for Certiorari will be styled "Pet. App. ___a." Citations to the Brief of the Petitioner will be styled "Pet. Br. ___." Citations to the record in the Supreme Court of Alabama below will be styled "Rec."

[2] Although respondents in this Court, the Gwins did not actively participate in the Alabama courts below on the issue of the arbitrability of the dispute, nor did they file a brief at the certiorari stage.

[3] The plan, which the Gwins had purchased four years earlier for $585.87 plus a $65.87 annual "extension charge" for the lifetime of the property, provided in relevant part:

> Upon transfer of ownership of the identified property, protection against subterranean termites may be continued upon the request of the new owner and upon payment of a contract transfer fee of $25.00. In addition, Terminix reserves the right to revise the annual extension charge upon transfer of ownership. In the event the new owner fails to request continued coverage or does not agree to pay the transfer fee or the revised annual extension charge, the Termite Protection Plan will terminate automatically as of the date of this change of ownership.

J.A. 75 (fifth paragraph).

"[I]t was explained to [the Dobsons] that there was an existing termite bond on the property that was being transferred," J.A. 63, although the Dobsons did not receive a copy of the termite bond they were being assigned. Rec. 991, 1014.

The termite bond assigned to the Dobsons had been purchased by the Gwins in 1987 from petitioner Allied-Bruce Terminix Companies, Inc. (trading as "Terminix Service"), through its nearby office in Daphne, Alabama. J.A. 75. Terminix Service is a franchisee of petitioner Terminix International Company ("Terminix International"), which provides the training, organizational and advertising support of the typical franchise operator, in exchange for a share of franchisee revenue. Rec. 106, 114, 1673, 1688-93. Although Terminix International insures customers against potential default on the service obligations of its franchisees, Rec. 1699,[4] according to Terminix Service employees, customers are made aware that they are "dealing with someone other than Terminix International," that "they are just dealing with us as local companies." *Id.*; *see also* 1476 (a local employee is "strictly an employee of Terminix Service").[5]

Prior to taking assignment of the termite bond at the closing on May 10, 1991, the Dobsons had "no conversations with anyone with either of those companies," Rec. 480; *see also* Rec. 445, 1646. The bargain reflected in the written contract

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[4] Terminix International also performs a background insurance function for its franchisees, helping them spread the costs of expensive treatment problems. Terminix International reimburses its franchisees for 80 percent of costs for repairing termite damage, after payment of an $1100 deductible per occurrence. Rec. 1694-96, 1698; *see also* Rec. 1476 (Terminix International "is like an insurance company").

[5] Consistent with this local focus, the manager of the Daphne office, his supervisor, and the vice president overseeing Alabama operations, are all located in Alabama, Rec. 1683-87, with the main office located in nearby Mobile. Rec. 1715. Employees of the Daphne branch are trained in the Mobile office. Rec. 1472, 1687. The branch's operations are licensed in Alabama and closely supervised by state regulators. Rec. 1604, 1727-33.

was straightforward: in exchange for an "annual extension charge" of $65.87 to be paid by the assignee (the amount of which might be revised), Terminix would provide termite protection for the lifetime of the residence located at 114 Fels Avenue in Fairhope, Alabama. J.A. 77. Specifically, Terminix promised to "provide the necessary service to protect the identified property against the attack of subterranean termites." J.A. 77 (first paragraph).[6]

Among the general conditions listed on the back of the form contract is an arbitration clause, stating in principal part: "The Purchaser and Terminix agree that any controversy or claim between them arising out of any provision of this agreement shall be settled exclusively by arbitration." J.A. 78 (¶ 9); *see also* Pet. Br. at 4 n.3 (full text).

Although the contract recites that "Terminix performs its services in accordance with the requirements of federal, state and local law," J.A. 78 (¶ 6), the contract is silent on the issue of what jurisdiction's law applies in determining the meaning and validity of the contract's provisions, including the arbitration clause. When the Dobsons entered into the contract in 1991, it was well settled under Alabama law that "a contract is governed by the laws of the state where it is made except where the parties have legally contracted with reference to the laws of another jurisdiction." *Cherry, Bekaert & Holland v. J. Charles Brown*, 582 So.2d 502, 506 (Ala. 1991). It was equally well settled that

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[6] The contract elaborates: "After this Plan is renewed beyond the initial contract term, Terminix will periodically reinspect the identified property and any further treatment found necessary will be performed free." J.A. 77 (second paragraph). The nature and limits of the covered services are defined more precisely as follows: "This Plan provides protection against new subterranean termite damage to the structure and contents. If new damage occurs during the contract term, Terminix will, upon notification and inspection, arrange for the necessary repairs and pay the cost of labor and materials not to exceed $100,000. New damage is damage associated with an active termite infestation. Unless live termites are found in the damaged area, the damage discovered is old damage and not covered under this Plan." J.A. 77 (fourth paragraph). In addition, various other "general conditions" are elaborated on the back of the form contract. J.A. 78.

"[t]he public policy of [Alabama] is to encourage arbitration and amicable settlements of disputes between parties; but public policy also holds void an agreement in advance to oust or defeat the jurisdiction of all courts, as to all differences between parties." *Wells v. Mobile County Board of Realtors, Inc.*, 387 So.2d 140, 144 (Ala. 1980). Nothing in the form contract that was assigned to the Dobsons purported to displace this rule. There was no indication that the Federal Arbitration Act might control the validity of the arbitration clause, nor any indication that the performance of the contract would involve interstate commerce in any way.

2. The Dispute.

The dispute between the parties began not with the termite bond assigned to the Dobsons, but with a report issued by Terminix to the Gwins three days before closing, on May 7, 1991, certifying that "[n]o visible evidence of infestation from wood destroying insects was observed." J.A. 5 (box 8(b)). This report was a service provided to the Gwins, who needed it to fulfill their sales contract, which required "a bonded and licensed termite control company" to certify "that a visual inspection by them indicates the dwelling is free from infestation by wood destroying insects." J.A. 66 (¶ 16). As the responsible Terminix Service vice president testified, this type of report — done to assess the condition of a residence for sale, not as part of termite eradication efforts — "doesn't have anything to do with the termite protection plan. It stands alone." Rec. 1780.

The report was issued by the head of the Daphne branch of Terminix Service. He admitted that when he did the inspection and issued the report he knew that he was doing it for the Dobsons' benefit and that the buyer "would be most interested in knowing if there are termites in the property." Rec. 1558-A. The Dobsons in fact relied on the report in proceeding with the closing. Rec. 451-52, 880-82.

One week after the closing, as they began preparations to move in within two weeks, the Dobsons discovered that the report was wrong, "[t]he whole thing [was] false," because the entire home was "absolutely infested with live termites." Rec.

888. In doing minor work on wall paneling, and then making more extensive checks, they discovered that there were "live termites swarming everywhere," Rec. 477, 998. Called in to inspect the house and begin extermination efforts that were to span months, the head of the Daphne office of Terminix Service said that the Dobsons "probably won't ever see this many termites again in one place." Rec. 498. Another Terminix Service employee admitted it was "a terrible problem." Rec. 1424. The Gwins' realtor agreed that the house was "totally and completely infested with live termites." Rec. 1235.

The Dobsons were shocked that their house was termite-ridden just days after professionals at Terminix had certified that there was no visible evidence of live termites. They investigated and learned that just six weeks before certifying the house as termite-free, Terminix employees had been at the house attempting to exterminate a massive swarm of termites. Rec. 1523-44, 1614-22, 1767. None of this had been revealed by Terminix. Even more seriously, the Dobsons discovered evidence that Terminix had affirmatively covered up its knowledge of signs of termite infestation that were in plain view on May 7, 1991, when Terminix issued its report.[7] Further, the Dobsons believed that the Gwins had also misled them about the house by failing to reveal the recent termite damage and the extensive eradication efforts. Rec. 583, 590, 1234.

Because Terminix and the Gwins had concealed their knowledge of the termite infestation, the Dobsons were led into buying a house that required immediate, massive termite eradication efforts, imposing serious financial and personal strain

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[7] Someone who had heard Terminix employees working on the house told Mr. Dobson that he would be "real surprised" at what he would find if he crawled under the house. Rec. 889, 1045. Mr. Dobson discovered that it was "clearly eaten up with live termites, from a "view that the Terminix inspector would have had to see," although that inspector had nonetheless marked on the report that underneath the house there was only "*old* termite damage with no live infestations." Rec. 889 (emphasis added); 1548. Not only was this damage plainly visible but, based on what the witness had seen and overheard, the Terminix employees had actually seen the problem but had failed to disclose it.

for many months.[8] On October 15, 1991, five months after this ordeal began, the Dobsons filed tort claims in Alabama state court against the Terminix companies and the Gwins. J.A. 7-10. In relevant part the Dobsons alleged that the Terminix companies had falsely and fraudulently "represented to the Plaintiffs that there was no visible evidence of infestation from wood destroying insects," J.A. 8, or, if they somehow lacked actual knowledge of the termites, that their inspection had been performed negligently. J.A. 9.

The defendants answered the complaint, and discovery and pretrial proceedings began. Eight months later, following inadequate repair efforts by Terminix under the termite bond and particularly a failure to cover all necessary repair-related costs, the Dobsons amended their complaint to allege breach of the termite bond.[9] A few days later, the Gwins filed a similar cross-claim against the Terminix companies. J.A. 55-57.

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[8] Because the termite treatments involved effectively tearing apart, treating and then rebuilding the entire inside of the house, the Dobsons were unable to unpack for eight to nine months until early 1992, going "from living on a mattress on the floor in the bedroom to having all the walls ripped out and living on a mattress on a floor in another bedroom with boxes all around us." Rec. 1047-48. The Dobsons' home was infamous in the small town to which they had just moved, becoming known as "the termite pit or the termite house" and, eventually, "the Money Pit," with people stopping by to say, "we heard about this, we know about you, we know what's going on." Rec. 579-81. The Dobsons were "humiliated, embarrassed, stressed, financially strapped," and "forced to live like pack rats for the majority of this time." Rec. 1047.

[9] Paragraph 6 of Count Four of the First Amended Complaint, filed June 25, 1992, alleges:

> That the Defendants, Terminix, have breached the terms of said Termite Protection Plan by failing to protect the identified property against the attack of subterranean termites, in that said dwelling has, since the purchase by the Plaintiffs, been infested throughout with live termites; and in that said Defendants, Terminix, did not arrange for all of the repairs rendered necessary by or pay for the same, but rather that the Plaintiffs were required to arrange for and pay for many of said repairs.

J.A. 53.

At this point, the Terminix companies invoked the Federal Arbitration Act, moving for an order compelling arbitration and for a stay of all litigation pending arbitration. The Terminix companies argued that the termite bond constituted the basis of all the claims asserted against them, J.A. 82-83, and that the termite bond was "a contract evidencing a transaction involving commerce" within the meaning of § 2 of the Act. J.A. 83-88.

In an effort to meet the statutory test, Terminix Service included an affidavit from its vice president in Mobile, Alabama, stating that Terminix Service was an Arkansas corporation and, further, that "[m]ost of the materials and equipment including specifically the chemical used to treat the home involved in this suit" had travelled from out of state before being used on the home. J.A. 72; *see also* J.A. 86. For its part, Terminix International rested on an officer's affidavit that it was incorporated in "a State other than Alabama" and operated elsewhere. J.A. 79-80; *see also* J.A. 86. Terminix International did not assert that it had engaged in *any* interstate activity in performing the termite bond; indeed, earlier it had stated that it had "no knowledge" of the Dobsons' situation. Rec. 116.

The Dobsons opposed application of the Act, arguing that "these connections with interstate commerce are too tenuous" to justify preemption of state law concerning a "purely local transaction" involving a home purchase between Alabama residents with an incidental assignment of a locally supervised termite bond. J.A. 93. Citing the Alabama Supreme Court's earlier reliance on *Metro Indus. Painting Corp. v. Terminal Constr. Co.*, 287 F.2d 382, 387 (2d Cir.), *cert. denied*, 368 U.S. 817 (1961) (Lumbard, C.J., concurring), the Dobsons urged that a focus on the "contemplation of the parties" was necessary. J.A. 93-95. Contrasting this case to one in which the contract "specifically called for" substantial interstate activity, J.A. 94, the Dobsons pointed out that they had "involved themselves in a routine consumer transaction with no notion whatever that they might be involved in interstate commerce," given that "[t]he Terminix [Service] office was in Daphne and there was no hint of any interstate activity." J.A. 95. The Terminix companies' attempt to force arbitration was denied. J.A. 96.

The Alabama Supreme Court granted discretionary review to consider the Terminix companies' claim that they had been improperly denied the benefit of § 2. The companies advanced the argument that, under § 2 of the Act, a "contract evidenc[es] a transaction involving commerce" whenever "that contract relates to or affects interstate commerce in any way," regardless of how the parties understood the transaction when they formed the contract. Brief of Appellants, at 19. Despite the meager interstate contacts laid out in their affidavits, the Terminix companies argued that "a party being from another state" or "purchase and transportation of materials from another state" was as a matter of law sufficient to trigger § 2's preemptive effect on state arbitration policy. *Id.*

The Dobsons urged that § 2 was not met because "there is no reason to believe that *at the time of contracting*, the parties to this consumer transaction contemplated any interstate activity" and that "[i]t is difficult to imagine a more 'local' transaction than employing someone to treat insects in one's home." Brief of Appellees at 13 (emphasis added). Focusing on what was "evidence[d]" by the contract, the Dobsons argued that it was irrelevant "that *it turns out* that the termite company which did the inspection had offices in states other than Alabama where one part of the form contract was executed and, at some point in the past, applied chemicals around the house which were purchased outside the state." *Id.* at 11 (emphasis added).

The Alabama Supreme Court rejected the Terminix companies' expansive view of the preemptive effect of § 2, reaffirming a pair of decisions in which it had embraced the "contemplation of the parties" test as more faithful to the text and purpose of the Act. *See* Pet. App. at 3a & n.1. In *Ex Parte Jones*, 628 So.2d 316 (Ala. 1993), the court had stressed that the plain language of § 2 requires that "*the agreement* that contains the pre-dispute arbitration provision must involve interstate commerce," finding in that agreement "no reference to any interstate matters." *Id.* at 317 (emphasis in original). In *Continental Grain Co. v. Beasley*, 628 So.2d 319 (Ala. 1993), however, the court made clear the evenhanded nature of this test, ruling that contracts "performed entirely within Alabama" will

nonetheless trigger § 2 if "[i]n performing their contractual obligations, the plaintiffs were directly engaging in the production of articles to be shipped in interstate commerce." *Id.* at 323.

Reviewing the record concerning whether the agreement between the parties involved interstate commerce, the court below found that "the evidence adduced by the Terminix companies does not establish that the parties contemplated substantial interstate activity when they entered the termite bond." Pet. App. 6a. The court rejected the idea that it could be enough under § 2 of the FAA "to show that one or more of the parties to the contract is located in another state," *id.*, focusing instead on what the parties contemplated in their agreement about "the *performance* of the bond obligations." *Id.* at 7a (emphasis in original). The fact that, as it turned out, "some materials used in fulfilling the bond obligations may have come from out-of-state suppliers" did not reasonably suggest, the court reasoned, that the parties "contemplate[ed] substantial interstate activity when they entered into the contract." *Id.* Therefore, the court held, the termite bond to which the Dobsons were a party was not "a contract evidencing a transaction involving commerce" within the meaning of § 2.

SUMMARY OF ARGUMENT

Section 2 of the Federal Arbitration Act of 1925 governs arbitration agreements in "contract[s] evidencing a transaction involving interstate commerce." 9 U.S.C. § 2. The Alabama Supreme Court correctly held that the Act does not apply to a termite bond purchased by Alabama homeowners from an Alabama termite services company.

I. This case arose in Alabama state court, not in federal court. As the Attorneys General of Alabama and 19 other States demonstrate in a brief *amici curiae* supporting respondents, the FAA should not be interpreted as governing proceedings in state court. This Court should overrule the decision in *Southland Corp. v. Keating*, 465 U.S. 1 (1984), to the extent that it held to the contrary and should adopt the construction of the FAA out-

lined in the dissenting opinion of Justice O'Connor in *Southland*, in which the current Chief Justice joined. The *Southland* Court was denied the benefit of full adversarial briefing and argument on the issue of whether the Act governs proceedings in state courts, primarily because in the California courts the *Southland* appellees had erroneously assumed that the Act applied. The States were not put on notice that the issue was before this Court and accordingly did not have a chance to participate.

The question is again presented, this time in more suitable fashion. The States persuasively demonstrate that the FAA does not contain the requisite "clear congressional statement" that would be necessary to justify the intrusion into state sovereignty and matters of traditional state concern, in light of this Court's recent decisions emphasizing the importance of federalism. *See New York v. United States*, 112 S. Ct. 2408 (1992), *Gregory v. Ashcroft*, 111 S. Ct. 2395 (1991), and *Will v. Michigan Dept. of State Police*, 491 U.S. 58 (1989). In adopting the FAA, Congress was repeatedly assured that the statute would *not* apply in state court, and lower courts and commentators unanimously adhered to that view for decades after the Act's enactment. The factors that normally lead this Court to decline to revisit issues of statutory construction are not present here. Indeed, this Court's decision in *Volt Information Sciences, Inc. v. Board of Trustees of Leland Stanford Junior University*, 489 U.S. 468 (1989), has already undermined the assumptions on which *Southland* was based.

II. Even if *Southland* were not overruled, the judgment below would still have to be affirmed, for even if the case below had arisen in federal court it would not be within the scope of the FAA. The termite bond at issue is not "a contract evidencing a transaction involving [interstate or foreign] commerce," within the meaning of § 2 of the FAA, 9 U.S.C. § 2.

The "contemplation of the parties" test developed by Chief Judge Lumbard in *Metro Indus. Painting Corp. v. Terminal Constr. Co.*, 287 F.2d 382, 387 (2d Cir.) (concurring opinion), *cert. denied*, 368 U.S. 817 (1961), best effectuates the statutory language and Congress' intent. Judge Lumbard's approach focuses on the *full* description of the type of contract to which

§ 2 refers: "a contract evidencing a transaction involving commerce." It is the *contract* which must evidence a transaction involving commerce. Accordingly, the appropriate question is whether, *at the time the contract was made*, reasonable persons in the parties' position would have contemplated more than *de minimis* interstate activity in carrying out the terms of the contract. The statutory test is not, as petitioners would have it, simply whether the parties' conduct *turns out* to "involve" or "affect" interstate commerce one way or another, even if such connections to commerce were wholly fortuitous or unforeseeable at the time of contracting.

The "contemplation of the parties" test, which has been used by many courts since it was developed over thirty years ago, is more faithful to the statutory language than is petitioners' proposal. The contemplation test recognizes that the key phrase — "a contract evidencing a transaction involving commerce" — is a single unit which must be construed as a whole. This Court has shared this view in *Bernhardt v. Polygraphic Co. of America*, 350 U.S. 198, 200 (1956), and more recently in *Perry v. Thomas*, 482 U.S. 483, 490 (1989), where this Court explained that § 2 applies only to "a contract evidencing interstate commerce." This Court's recognition that it is the *contract*, not the *transaction*, which must "evidence interstate commerce" strongly supports the "contemplation of the parties" test and undermines petitioners' novel proposal.

Indeed, petitioners' argument would require this Court to overrule the interpretation of § 2 set forth in *Bernhardt* and never doubted since. *Bernhardt* held that the Act did not apply to an employment contract made by parties residing in New York, even though it provided for one of the parties to change his state of residence and perform his employment obligations in the new state. Petitioners' view of § 2 of the FAA is squarely foreclosed by the holding of *Bernhardt*.

The "contemplation of the parties" test provides a workable approach that permits parties that are plainly engaged in interstate commerce to invoke the provisions of the FAA, while ensuring that unsuspecting consumers and other unsophisticated parties do not find themselves bound by the Act. The test thus honors the

reasonable expectations of the parties, which this Court identified as a key objective of the FAA in *Volt Information Sciences*. Petitioners' approach would defeat the reasonable expectations of the parties, by sweeping into the ambit of the FAA contracts whose parties did not expect to be subject to the jurisdiction of the Act.

Moreover, the "contemplation of the parties" test is consistent with Congress' understanding of Commerce Clause jurisprudence in 1925. Congress was on notice that, in construing statutes regulating contractual relationships, the courts would look to the contemplation of the parties to determine the nexus to interstate commerce.

III. Even if the "contemplation of the parties" test were rejected and petitioners' proposal adopted, the judgment below would still have to be affirmed. It is highly significant that § 2 of the FAA uses the phrase "involving commerce" rather than "affecting commerce." *Bernhardt* indicates that § 2 does *not* extend to the limits of Congress' power under the Commerce Clause, and that decision is still good law. The FAA was adopted in 1925 against the background understanding that the word "involve" has a much narrower meaning than the word "affect." By using the phrase "involving commerce," Congress meant to include only conduct that is actually within the "current" or "flow" of interstate commerce. The termite bond at issue does not qualify under this test.

ARGUMENT

I. THIS COURT SHOULD GRANT THE REQUEST OF THE *AMICI* STATES FOR A HOLDING THAT THE FEDERAL ARBITRATION ACT DOES NOT GOVERN PROCEEDINGS IN STATE COURT

This case provides a suitable vehicle for this Court to revisit an issue prematurely addressed in *Southland Corporation v. Keating*, 465 U.S. 1 (1984), without the benefit of any briefing or even oral argument: the issue of whether the FAA governs proceedings in state court in the first place. This issue

was never properly joined in *Southland* and therefore should be considered now, based on the Brief *Amici Curiae* of the Attorneys General of Alabama and 19 other States in Support of Respondents ("States' Br."). The States decisively demonstrate the profound flaws in the *Southland* majority opinion of Chief Justice Burger, joined by Justices Brennan, White, Marshall, Blackmun and Powell, and explain why the dissenting opinion in *Southland*, 465 U.S. at 21-36 (O'Connor, J., joined by Rehnquist, now C.J., dissenting), was clearly correct in its reading of the statute.

The factors that normally lead this Court to avoid revisiting issues of statutory construction are not present here, for this case involves fundamental issues of federalism on which the States were not heard in 1984, and on which the controlling jurisprudence has shifted in the past decade.

In *Southland*, the state-court private plaintiffs who appeared as appellees had stipulated in the lower courts that the FAA applies in state court. *See* Brief of Appellees in No. 82-500 (filed June 6, 1983) at 25 n.30; *Keating v. Superior Court*, 31 Cal.3d 584, 604, 645 P.2d 1192, 1203, 183 Cal. Rptr. 360, 371-72 (1982). The appellees sought affirmance of the judgment denying arbitration only on the basis that the FAA did not preempt California's targeted statutory scheme designed to protect franchisee owners. The appellees continued to ignore the issue even after one justice, at the beginning of oral argument, suggested to the appellant that the legislative history on the issue was "pretty clearly against" the idea that the Act applies in state courts, and that the Court's previous comment to the contrary in *Moses H. Cone Memorial Hospital v. Mercury Construction Corp.*, 460 U.S. 1, 24, 26 n.34 (1983), was clearly dictum as *Moses H. Cone* came from a federal court. Oral Argument Transcript, No. 82-500, Oct. 4, 1983, at 7-8.

In *Southland*, this Court was denied the benefit of adversarial briefing, in particular the benefit of a brief from the States. *See* States' Br. at 1-2 & n.2. Moreover, the approach to statutory interpretation used in *Southland* has been outmoded by key precedents during the past decade. The *Southland* majority

held the FAA to have a massive preemptive effect in all state-court proceedings despite the plain text of the Act addressing only "courts of the United States" (§ 3) and "United States district court[s]" (§ 4), and the admission that "the legislative history is not without its ambiguities." 465 U.S. at 12.

The *Southland* majority's core supposition that "Congress had in mind something more than making arbitration agreements enforceable only in the federal courts," *id.*, obviously cannot survive the scrutiny of this Court's "clear statement" jurisprudence increasingly emphasized subsequent to *Southland*. *See* States' Br. at 8-9. Moreover, the opinion for the Court delivered by the Chief Justice in *Volt Information Sciences, Inc. v. Board of Trustees of Leland Stanford Junior University*, 489 U.S. 468, 477 (1989), noting that the FAA lacks an "express pre-emptive provision" and does not "reflect a congressional intent to occupy the entire field of arbitration," is in obvious tension with *Southland*. In sum, there are ample reasons for this Court to take this opportunity to overrule the precipitate and ill-advised *Southland* holding that the FAA governs state-court proceedings. That the issue was not litigated and decided below is entirely understandable and of course presents no barrier to this Court's review. *See* States' Br. at 5 n.8.

However, this Court need not revisit the *Southland* issue in order to affirm the judgment of the Alabama Supreme Court because, even if this case had arisen in federal court, the FAA would not apply to the termite bond that was assigned to the Dobsons. For nothing in the text or legislative history of § 2 suggests that the termite bond is "a contract evidencing a transaction involving commerce."

II. SECTION 2's "CONTRACT EVIDENCING" LANGUAGE PLAINLY REQUIRES A COURT TO DETERMINE BASED ON THE CONTRACT BETWEEN THE PARTIES WHETHER THEY CONTEMPLATED ENGAGING IN "A TRANSACTION INVOLVING COMMERCE"

The "contemplation of the parties" standard employed by the court below in analyzing § 2 of the Act has been relied on by many courts[10] and flows naturally from the plain language of § 2, supplemented by a practical understanding of the purposes of the Act. As explained by Judge Lumbard in his influential opinion in *Metro Indus. Painting Corp. v. Terminal Const. Co.*, 287 F.2d 382, 387 (2d Cir.) (Lumbard, C.J., concurring), *cert. denied*, 368 U.S. 817 (1961), such a test is necessitated by Congress's very specific description of the type of contract that falls under § 2's ambit.

Judge Lumbard was careful to focus on the *full* description of the type of contract Congress targeted in § 2: "a contract evidencing a transaction involving commerce." As he pointed out:

> The statute does not purport to affect arbitration provisions in *all* contracts involving commerce; it puts its stamp only on such provisions when incorporated in contracts *evidencing a transaction* involving commerce.

Id. at 387 (first emphasis added). From the "contract evidencing" language selected by Congress, it was obvious to Judge Lumbard that a judge's task is not to look at a transaction between parties retrospectively, asking "what in fact happened." *Id.* Rather, a judge must determine "what was in the contemplation of the parties as manifested in their written agreement." *Id.*

As Judge Lumbard further pointed out, given § 2's rigorous, almost "formalistic" requirement that the contract at

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[10] *See* Brief *Amicus Curiae* of the Southern Poverty Law Center in Support of Respondents ("So. Poverty Law Ctr. Br."), at 8-9 & n.10 (listing selected cases).

issue "evidenc[e] a transaction involving commerce," in looking only to the words of the statute "we might be justified in limiting the effect of the act to only those contracts which, *on their face*, reveal that some interstate transaction is to take place." *Id.* (emphasis added). Such a close focus on the text of § 2, Judge Lumbard noted, would restrict the preemptive effect of the Act "upon essentially local transactions." *Id.* At the same time, it appears that this narrow reading of § 2 would have fully accomplished the objectives behind the Act held by the merchants who helped draft it and who appeared before Congress in 1925 to lobby for its passage — merchants who dealt with interstate commodities shipments and whose contracts routinely made clear, on their face, the interstate transaction involved.[11]

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[11] As Justice Black summarized the legislative history several years after Judge Lumbard's opinion, in his dissent to *Prima Paint v. Flood & Conklin Mfg. Co.*, 388 U.S. 395 (1967):

> The principal support for the Act came from trade associations dealing in groceries and other perishables and from commercial and mercantile groups in the major trading centers. Practically all who testified in support of the bill before the Senate subcommittee in 1923 explained that the bill was designed to cover contracts between people in different States who produced, shipped, bought, or sold commodities. The same views were expressed in the 1924 hearings. When Senator Sterling suggested, "What you have in mind is that this proposed legislation relates to contracts arising in interstate commerce," Mr. Bernheimer, a chief exponent of the bill, replied: "Yes; entirely. The farmer who will sell his carload of potatoes, from Wyoming, to a dealer in the State of New Jersey, for instance."

Id. at 409 n.2 (Black, J., dissenting) (citations omitted). *See also* So. Poverty Law Ctr. Br. at 4-5 & n.8. Although the majority in *Prima Paint* did not dispute Justice Black's explication of the genesis of the Act, it rejected Justice Black's argument from that premise that the FAA should "apply only to 'contracts between merchants for the interstate shipment of goods.'" 388 U.S. at 401 n.7 (quoting dissent). But the *Prima Paint* majority did not embrace the present petitioners' reading of § 2 of the FAA. Rather, the majority indicated merely that the Act applied to an agreement between two business corporations concerning "the purchase of an entire interstate paint business and its re-

Judge Lumbard elected to construe § 2 of the Act more broadly than its plain language would perhaps dictate, based on a "more realistic appraisal of the ends Congress wished to serve." 287 F.2d at 387. However, Judge Lumbard was careful to remain faithful to the text of § 2. It was clear to him that "Congress was *not* seeking to regulate and control activity affecting commerce," preempting the field of arbitration with an "intent to affect all contracts possessing certain interstate elements." *Id.* (emphasis added). Rather, Congress "was providing for those engaged in interstate transactions an expeditious extra-judicial process for settling disputes," and "the purpose of the act was to assure those who desired arbitration that their expectations would not be undermined by federal judges." *Id.*

The required focus on the parties' expectations meant, of course, that the ultimate issue under § 2 is the contemplation of the parties. As Judge Lumbard explained:

> The significant question, therefore, is not whether, in carrying out the terms of the contract, the parties *did* cross state lines, but whether, at the time they entered into it and accepted the arbitration clause, they *contemplated* substantial interstate activity. Cogent evidence regarding their state of mind at the time would be the terms of the contract, and if it, on its face, evidences interstate traffic . . . the contract should come within § 2. In addition, evidence as to how the parties expected the contract to be performed and how it was performed is relevant to whether substantial interstate activity was contemplated.

Id.[12]

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establishment and operation in another State." *Id.* at 402 n.7. Such a contract would fall within any conception of the Act's scope.

[12] After articulating this clear and sensible test designed to defend the parties' reasonable expectations, Judge Lumbard found the case before him

Contrary to assertions of petitioners and their *amici*, Judge Lumbard's analysis is not the antiquated relic of a bygone era. Rather, it is a workable standard that has stood the test of time for over 30 years and continues to be used by many courts today. *See* note 10, *supra*. Judge Lumbard's analysis demonstrating that Congress was not seeking to preempt the arbitration field by regulating all contracts affecting commerce matches a similar ruling by this Court five years ago, announced by the Chief Justice in *Volt Information Sciences v. Board of Trustees of Leland Stanford Jr. Univ.*, 489 U.S. 468 (1989), holding that "[t]he FAA contains no express pre-emptive provision, nor does it reflect a congressional intent to occupy the entire field of arbitration," *id.* at 477, and that "parties are generally free to structure their arbitration agreements as they see fit." *Id.* at 479. Notably, petitioners have ignored *Volt Information* in all three briefs filed in this Court. Moreover, petitioners ignore that even the majority opinion in *Southland Corp. v. Keating*, 465 U.S. 1, 13 (1984), endorsed Judge Lumbard's view that the Act was designed to protect parties' contractual expectations.

Further, petitioners' entire effort to overturn Judge Lumbard's test rests on a linguistic absurdity. The obvious meaning of the words of § 2, as Judge Lumbard emphasized, is that § 2 does not apply unless the contract at issue "evidenc[es] a transaction involving commerce." The phrase is a single unit which must be construed as a whole. This Court adopted that very construction of § 2 in both of its cases construing the nature of the contracts covered by § 2. In *Bernhardt v. Polygraph Co. of America*, 350 U.S. 198 (1956), this Court made clear that the phrase in question must be read as a unified whole:

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simple to resolve: the face of the contract at issue showed that two companies doing business in New York entered into a subcontractor agreement on a Florida construction project, and the performance of the contract had involved substantial travel from New York to Florida, so that "it appear[ed] reasonably clear that the parties anticipated substantial interstate traffic." *Id.* at 388.

> Section 2 makes "valid, irrevocable, and enforceable" only two types of contracts: those relating to a maritime transaction and those involving commerce. No maritime transaction is involved here. Nor does this contract *evidence "a transaction involving commerce"* within the meaning of § 2 of the Act.

Id. at 200 (emphasis added). *See also Prima Paint,* 388 U.S. at 401 (reaffirming this aspect of *Bernhardt*).

Despite *Bernhardt*'s straightforward statement that under § 2 the contract must evidence a very particular kind of transaction — "a transaction involving commerce" — petitioners urge a different reading of § 2, a reading that is essential to their effort to dislodge the "contemplation of the parties" test. In petitioners' view, the words "contract evidencing" modify *only* the next two words in § 2, "a transaction." Pet. Br. at 15, 24. Once a judge has consulted the contract long enough to confirm that it evidences "a transaction," we are told, the judge can set the contract aside. The only remaining question is whether the judge can find, somewhere in the record, that some part of the transaction *as ultimately carried out* crossed state lines and thereby supposedly "involv[ed] commerce." What the parties *contemplated* about interstate activity when they made the contract is irrelevant, because under petitioners' proposed construction the contract itself need not evidence "a transaction involving commerce" — just "a transaction." "Taken at face value," petitioners argue, "the contract must be evidence of the *transaction*, not of the 'commerce' to which it applies." Pet. Br. at 15 (emphasis in original). *See also* Pet. Br. at 24 ("the contract must be evidence of the transaction").

The linguistic absurdity that pervades petitioners' entire line of argument is that, by definition, *every* contract evidences a transaction, because every contract *is* a transaction. *See, e.g.*, Black's Law Dictionary 1166 (2d ed. 1910) ("'Transaction' is a broader term than 'contract.' A contract is a transaction, but a transaction is not necessarily a contract"); 2 Bouvier's Law Dictionary (rev. ed. 1897) (ed. F. Rawle) ("The term transaction

is a broader one than contract"); *Farnsworth v. Duffner*, 142 U.S. 43, 48 (1891) (quoting 2 Pomeroy's Equity, which speaks of a "contract or *other transaction*") (emphasis added); *Embrey v. Southern Gas & Electric Corp.*, 63 So.2d 258, 263 (1953) ("[w]hile every contract is a transaction, every transaction is not a contract"). Because the phrase "contract evidencing" can have no meaning if it refers only to "a transaction," it must be seen as referring to the unitary concept of "a transaction involving commerce" contained in § 2.

Of course, that is exactly how this Court treated these words in *Bernhardt* and *Prima Paint*, a point petitioners would prefer to avoid facing. For if petitioners' interpretation of the words "contract evidencing" were adopted, *Bernhardt* would have to be overruled. In *Bernhardt*, all nine Justices agreed that the employment contract of a plant supervisor, made in New York with a New York corporation and performed in Vermont, was not a "contract evidencing a transaction involving commerce," within the meaning of § 2. *See* 350 U.S. at 200-201; *see also id.* at 208 (Frankfurter, J., concurring) (agreeing that "the Act is not here applicable"). Only the "contemplation of the parties" test, or a similarly narrow reading of § 2, can explain the holding of *Bernhardt*.[13]

Petitioners' *amici* candidly acknowledge that, under their approach, *Bernhardt* would have to be overruled. *See* Br. American Arbitration Ass'n at 7-8 n.1. The most petitioners can say is that the result in *Bernhardt* is "somewhat surprising." Pet. Br. at 21 n.12. But when a proposed theory does not fit this

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[13] Judge Lumbard's explanation of the "contemplation of the parties" test is in harmony with this Court's result in *Bernhardt*. He cautioned:

> The fact that it is necessary for one party to cross state lines in order to fulfill obligations arising out of the contract should not by itself bring the arbitration clause within the reach of the federal statute. The Arbitration Act should apply only when the parties know or have reason to believe that the performance of the contract will require substantial interstate movement.

287 F.2d at 388 (citations omitted).

Court's prior decisions, it is usually the former — not the latter — that must be rejected. *Bernhardt's* construction of § 2, which came much closer in time to the enactment of the FAA than does petitioners' attempt to rewrite the Act 70 years after its passage, is surely entitled to deference.[14]

Petitioners' final effort to dislodge the "contemplation of the parties" test hinges on the claim that it is unduly "subjective." Pet. Br. at 24. In reality, as Judge Lumbard himself articulated the test (*see* pp. 16-17, *supra*), and as one *amicus* has touched upon (*see* So. Poverty Law Ctr. Br. at 7), the test is a largely objective one inquiring into the reasonable expectations of the parties to a contract. More fundamentally, to the extent that the test does address the subjective contemplation of the parties at the time of contracting, it is faithful to the statutory text and to the underlying purpose of the FAA, *see Volt Information Sciences*, 489 U.S. at 478-79 (FAA protects reasonable expectations of parties).

It is hardly "inexplicable" for Congress to have wanted the application of the Act "to depend in every case upon what the parties *subjectively* understood." Pet. Br. at 24 (emphasis in original). The entire structure of contract law is aimed at

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[14] There can be no claim that *Bernhardt* has been undermined by subsequent cases involving the FAA. This Court's recent cases, such as *Shearson/American Express Inc. v. McMahon*, 482 U.S. 220 (1987), and *Rodriguez de Quijas v. Shearson/American Express, Inc.*, 490 U.S. 477 (1989), have concerned securities trading, large corporate transactions, and other matters plainly involving interstate commerce under any understanding of the term. None of the Court's recent cases has examined in any detail the key language of § 2: "contract[s] evidencing a transaction involving commerce." The brief references that do exist only support the *Bernhardt* construction of § 2 giving independent content to its "evidencing" language. For example, *Perry v. Thomas*, 482 U.S. 483, 490 (1989), lauded by petitioners for a passing comment about "the pre-emptive effect of the Federal Arbitration act," on contracts to which it is found to apply, with regard to conflicting state law (*see* Pet. Br. at 6, 8, 11, 17), itself recognizes that § 2 only applies to "a contract *evidencing* interstate commerce." *Id.* at 489 (emphasis added). This Court's recognition that the contract *itself* must evidence interstate commerce is contrary to petitioners' theory, *see* Pet. Br. 15, 24, and strongly supports the "contemplation of the parties" test.

effectuating the parties' understandings as to a contract's scope and contents. Consequently, "the FAA's primary purpose [is] ensuring that private agreements to arbitrate are enforced according to their terms. Arbitration under the Act is a matter of consent, not coercion, and parties are generally free to structure their arbitration agreements as they see fit." *Volt Information Sciences*, 489 U.S. at 479.

The "contemplation of the parties" test is also perfectly consistent with Congress' understanding of background Commerce Clause jurisprudence when the Act was passed in 1925. Congress was on notice that, in construing statutes regulating contractual relationships among parties involved in commerce, the courts would look to the contemplation of the parties to determine whether they intended to participate in interstate as opposed to intrastate commerce. Three examples illustrate the point. In 1906 this Court refused to apply the Sherman Act to a contract for the sale of vessels that contemplated the vessels' being transported between two Ohio cities, despite the fact that the vessels sailed briefly outside Ohio on water "over soil belonging to Kentucky." *Cincinnati, Portsmouth, Big Sandy and Pomeroy Packet Co. v. Bay*, 200 U.S. 179, 183 (1906). This Court ruled that the statute did not cover this contract, despite the direct contact with another state, given what the parties had contemplated and what their contract evidenced. This Court noted that "it does not appear on the record that the contract necessarily contemplated commerce between the States" at all, and ruled that "[t]he contract, in what it especially contemplates, is a domestic contract," with the route to be taken "between Ohio ports," and held that "[t]he chief and visible object of its provisions has nothing to do with commerce among the States." *Id.* at 183-84.

In 1923, just two years before Congress enacted the FAA, this Court considered whether the transactions of New York film distributors with a Nebraska motion picture exhibitor constituted interstate commerce even though the distributor's films were delivered to the exhibitor through agencies in Nebraska. In holding that these transactions *were* interstate commerce, this Court was careful to note that "[t]he contracts with these

distributors contemplated and provided for transactions in interstate commerce." *Binderup v. Pathe Exchange, Inc.*, 263 U.S. 291, 312 (1923) (emphasis added). In fact, in language that fits perfectly with Judge Lumbard's "contemplation of the parties" test, this Court began its inquiry into whether the transactions at issue were interstate commerce with the observation that "[t]he film contracts were between residents of different States and contemplated the leasing by one to the other of a commodity manufactured in one State and transported *and to be transported to* and used in another." *Id.* at 309 (emphasis added).

Finally, in 1925, the very year that Congress enacted the FAA, this Court further emphasized the importance of the parties' contemplation with respect to commercial transactions, in holding that the activities of a Missouri corporation in Arkansas were sufficiently *intrastate* so that an Arkansas law fining a foreign corporation for failing to register with the state was not repugnant to the Commerce Clause. As this Court explained, "[f]rom the beginning, transactions local to Arkansas were contemplated." *Kansas City Structural Steel Company v. Arkansas*, 269 U.S. 148, 151 (1925).

It would therefore have been completely natural for Congress to expect that application of the FAA would depend in part on the contemplation of the parties to the contract.

III. SECTION 2's "A TRANSACTION INVOLVING COMMERCE" LANGUAGE PLAINLY REQUIRES A COURT TO DETERMINE WHETHER THE TRANSACTION AT ISSUE IS ACTUALLY PART OF THE "CURRENT" OR "FLOW" OF INTERSTATE COMMERCE

Even if this Court were to decline this opportunity to overrule *Southland*'s ill-advised extension of the FAA to govern proceedings in state court, and even if this Court were to adopt the linguistic absurdity offered by petitioners and thereby reject the "contemplation of the parties" test, affirmance of the judgment below would still be warranted. For there would still remain the issue of what § 2 means when it refers to "a transaction involving commerce."

Petitioners' theory is simple: In enacting the FAA, Congress drew in part on its Commerce Clause powers. Pet. Br. at 11, 13. "[I]t is now accepted" — that is, post-1937 — that these powers extend to "'activities affecting commerce.'" *Id.* at 12 (citation omitted). One of many definitions of "involving" found in a 1992 dictionary is "'[t]o influence or affect.'" Pet. Br. at 14 (citation omitted). Thus, petitioners contend that "the term 'involving commerce' is sufficiently close in meaning to signal the same intent" as "affecting commerce." Pet. Br. at 15 n.6.[15] Petitioners conclude all of the above from an initial assumption that, when Congress exercised its powers over commerce in 1925, "there is no reason to think that [it] . . . left some (undefined) portion of its power unexercised." Pet. Br. at 16. Petitioners also sprinkle their argument with liberal doses of language from past FAA cases describing the broad preemptive effect of the FAA in sweeping aside barriers to arbitration once the Act *is* found to apply to a given contract. *See, e.g., id.* at 6; *compare* note 14, *supra* (observing that petitioners' most-cited case on this point, *Perry v. Thomas*, 482 U.S. 483 (1989), actually reaffirms the "evidencing" requirement of § 2). Petitioners repeatedly suggest that this Court has already held that § 2 extends to all transactions that Congress can constitutionally reach under the Commerce Clause.

What petitioners refuse to confront is that in fact this Court has already construed § 2 as *not* reaching to the limits of the Commerce Clause, a decision that remains good law. As already noted, *Bernhardt v. Polygraphic Co. of America*, 350 U.S. 198 (1956), held that a transaction clearly within Congress's power to regulate under the Commerce Clause — a plant supervisor's agreement to relocate to another state in order to perform contractual duties — was nonetheless not "a contract evidencing a transaction involving commerce" under § 2. Thus, this Court has already ruled against the principal argument advanced by petitioners (Pet. Br. at 11-23), that § 2 governs all transactions Congress is constitutionally permitted to regulate. Petitioners

[15] That assumption is fundamentally incorrect. *See* note 16, *infra*.

have not even attempted to make a case for overruling *Bernhardt*. The best they can manage is to describe its unanimous holding as "surprising" and to suggest that the only reason that § 2 was construed narrowly was to avoid an *Erie* problem. Pet. Br. at 21 n.12. But the supposed motivation for the holding in *Bernhardt* is irrelevant. There is no basis for overruling *Bernhardt*, nor do petitioners suggest one. *See* pp. 20-21 & n.14, *supra*.[16]

Setting aside petitioners' untenable theory that § 2 was intended to encompass all transactions within Congress' commerce powers, there is only one remaining way to read § 2: as the words "transaction involving commerce" would have been understood in 1925, when Congress enacted the FAA. It is settled, of course, that the terms of a statute are to be construed according to their meaning at the time of enactment. *E.g., Will v. Michigan Dept. of State Police*, 491 U.S. 58, 69 & n.9 (1989) (engaging in "an examination of authorities of the era" in which

[16] Even if this Court were willing to revisit *Bernhardt* and consider the possibility that Congress, in enacting the FAA in 1925, intended to exercise its Commerce Clause powers to the constitutional limit, petitioners and their *amici* have failed to address the issues that would be pivotal to this inquiry. It is not enough simply to posit, as petitioners do, that "the term 'involving commerce' is sufficiently close in meaning to signal the same intent" as "the term 'affecting commerce,'" Pet. Br. at 15 n.6, or to draw a hurried analogy to the Sherman Act, as one of petitioners' *amici* does. *See* Brief of American Arbitration Association as *Amicus Curiae* at 12-13. As this Court noted in *Federal Trade Comm'n v. Bunte Bros.*, 312 U.S. 349, 351 (1941), where Congress exercises its commerce powers over "activities which in isolation are merely local, it has normally conveyed its purpose explicitly," and "a due regard for a proper adjustment of the local and national interests" requires in such circumstances that statutes not be construed "beyond the obvious meaning of language unless otherwise the purpose of the Act would be defeated." *Id. See also id.* at 355; *Gulf Oil Corp. v. Copp Paving Co.*, 419 U.S. 186, 195-99 (1974); So. Poverty Law Ctr. Br. at 6 n.6. This Court recently employed a similar principle in unanimously rejecting a statutory construction that failed to evince a "clear and manifest congressional purpose" to displace state substantive protections by increasing the scope of mandatory labor arbitration. *See Hawaiian Airlines, Inc. v. Norris*, 62 U.S.L.W. 4537, 4540 (U.S. June 20, 1994).

42 U.S.C. § 1983 was adopted in order to construe the meaning of "person").

By the year the FAA was enacted, this Court had at least twice explicitly compared the concept of a transaction "involving" commerce to the concept of a transaction "affecting" commerce and had drawn a sharp distinction between the two. In *United Mine Workers v. Coronado Coal Co.*, 259 U.S. 344, 407-08 (1922), this Court reaffirmed its position that coal mining and manufacturing did not constitute "interstate commerce," and thus that a coal miners' strike shutting down a local coal mine did not involve "a direct obstruction" of commerce, although it "may affect it by reducing the amount of coal to be carried in that commerce." Addressing the nature of Congress's power over commerce, the Court noted

> a distinction to be drawn in cases which do not *involve interstate commerce intrinsically* but which may or may not be regarded as *affecting* interstate commerce so directly as to be within the federal regulatory power.

Id. at 410 (emphasis added). In 1925 this Court reaffirmed the distinction between transactions that "involve" commerce and thus were clearly within Congress' power, and those that "affect" commerce, and thus were more dubious subjects of regulation. *See United Leather Workers v. Herkert*, 265 U.S. 457, 466-71 (1925). Summarizing its Commerce Clause jurisprudence, the Court confirmed that Congress' power over activities that "involve interstate commerce intrinsically" concerned "the practical conception of interstate commerce as a flowing stream from one State to another formed by a regular course of business." *Id.* at 467.

Given this Court's caselaw circa 1925 concerning the powers Congress had in its possession over commerce, the phrase "a transaction involving commerce" should be defined to mean a transaction between businesspersons who are part of the "flowing stream" of commerce as the term "commerce" was understood in 1925. That interpretation is fully consistent with the relevant legislative history concerning the objectives behind

the Act. *See* note 11, *supra*; So. Poverty Law Ctr. Br. at 4-5 & n.8. There is no basis for concluding that in 1925 Congress was attempting to draw on uncertain powers over undefined transactions that might somehow "affect" commerce. Rather, by its careful choice of language in § 2 Congress was drawing only on its power to regulate transactions that "involve interstate commerce intrinsically," as had been previously defined by this Court.

If § 2 is construed in this manner, then the termite bond to which the Dobsons and the Terminix companies are parties cannot qualify as "a transaction involving commerce." The termite bond was merely a personal contract that insured the Dobsons against the costs of termite damage and extermination, and all services under it were performed locally. *See* pp. 2-6, *supra*. That the transaction included "parties in different states" and "materials brought from one state to another," Pet. Br. at 28, does not mean that it "involv[ed] commerce" within the meaning of § 2.[17]

In the end, petitioners and their *amici* are left to argue that the FAA should not be "frozen" to embody Congress' intention in 1925, but rather "should be interpreted in view of modern, more expansive notions" of Congress' powers. Br. of American Arbitration Ass'n at 13. Petitioners' *amici* go so far as to claim that it would be "wholly arbitrary" to construe the Arbitration Act "on the basis of the particular words that Congress used" rather than on the basis of Congress' supposed intent to extend the FAA to the limits of the Commerce Clause. *Id.* at 12-13.

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[17] The pertinent caselaw on this subject was well settled by the time the FAA was enacted. *See, e.g., Ware and Leland v. Mobile County*, 209 U.S. 405, 411 (1908) ("contracts between citizens of different States are not the subjects of interstate commerce . . . where the contract itself is to be completed and carried out wholly within the borders of a State, although such contracts incidentally affect interstate trade"); *Hooper v. California*, 155 U.S. 648, 654 (1895) ("personal contracts between parties . . . though the parties may be domiciled in different States . . . are . . . local transactions, and are governed by the local law"). *See also New York Life Ins. Co. v. Deer Lodge County*, 231 U.S. 495, 510 (1913) ("contracts of insurance are not commerce at all, neither state nor interstate").

But, for better or worse, statutes must be read as "freezing" into law the memorialized intentions of the particular legislature that enacted them. They cannot be rewritten 70 years after the fact based on insupportable conjecture about Congress' inchoate and unexpressed intentions.

Petitioners' theory of statutory interpretation might have force where a legislature expressly provides that its enactment goes to the limit of what the Constitution permits, as is the case with some state long-arm statutes, or where the legislative intent to do so is equally clear, as in the case of the Sherman Act.[18] But the language of the FAA — which is confirmed by the relevant legislative history — leaves no doubt that the "involving commerce" test was adopted so that the scope of the FAA would be limited to transactions between merchants, interstate shippers, national or regional companies, and others directly engaged in the "flowing stream" of commerce.

CONCLUSION

The judgment of the Alabama Supreme Court should be affirmed.

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[18] *See, e.g., Summit Health, Ltd. v. Pinhas*, 111 S. Ct. 1842, 1846 n.7 (1991) ("[t]he floor debates on the Sherman Act reveal, in Senator Sherman's words, an intent to 'g[o] as far as the Constitution permits Congress to go'") (quoting 20 Cong. Rec. 1167 (1889)).

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IN THE
Supreme Court of the United States
OCTOBER TERM, 1994

ALLIED-BRUCE TERMINIX COMPANIES, INC., and TERMINIX INTERNATIONAL COMPANY,
Petitioners,

v.

G. MICHAEL DOBSON, WANDA C. DOBSON, STEVEN GWIN and JAN GWIN,
Respondents.

On Writ of Certiorari to the Supreme Court of Alabama

REPLY BRIEF FOR PETITIONERS

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REPLY BRIEF FOR PETITIONERS

In construing Section 2 of the Federal Arbitration Act, 9 U.S.C. § 2, this Court does not write upon a blank slate. During the past four decades, the Court has established that "[i]n enacting § 2 of the federal Act, Congress declared a national policy favoring arbitration and withdrew the power of the states to require a judicial forum for the resolution of claims which the contracting parties agreed to resolve by arbitration." *Southland Corp. v. Keating*, 465 U.S. 1, 10 (1984); *Perry v. Thomas*, 482 U.S. 483, 489 (1987). With respect to the scope of Section 2, the Court has held that it sets forth federal substantive law enacted pursuant to the congressional power over interstate commerce (*Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, 388 U.S. 395 (1967)); that it applies in state as well as federal courts (*Southland Corp.*); that

it applies not just to arbitration of disputes between merchants (*Prima Paint*) but to arbitration of a wide variety of statutory and common law claims (*e.g., Gilmer v. Interstate/Johnson Lane Corp.*, 111 S. Ct. 1647 (1991)); and that it mandates enforcement of arbitration agreements despite assertions of unequal bargaining power, unless the inequality would be grounds for the revocation of *any* contract (*Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 627 (1985)).

Respondents and their *amici curiae* accept very little of this established law. Although they reluctantly concede that Congress enacted Section 2 in an exercise of its commerce power, they insist that Congress, for unexplained reasons, exercised only a fraction of that power, and they contend—urging the overruling of *Southland Corp.*—that Section 2 should not apply at all in state courts. *See* Resp. Br. at 12-14; Brief *Amici Curiae* of the Attorneys General of the State of Alabama, Alaska, et al. at 1-20 ("Ala. Br."). At various other points, they suggest that the Act should not apply to transactions with consumers and, in any event, should never apply to parties with different degrees of bargaining power. Resp. Br. at 26-28; Ala. Br. at 19; Brief *Amicus Curiae* of the Southern Poverty Law Center at 4-5 ("SPLC Br."). Then, in keeping with their general hostility towards arbitration, respondents and their *amici curiae* press for a reading of Section 2 that would limit its jurisdictional reach as much as possible, allowing States to void agreements to arbitrate unless the parties also agreed about the extent of interstate commerce involved in their transaction. Resp. Br. at 15-23; SPLC Br. at 6-11. Finally, as a fallback position, they argue that the Act should apply only to transactions in "the 'current' or 'flow' of interstate commerce," rather than to transactions generally falling within the congressional power over interstate commerce. Resp. Br. at 23-28. As we briefly discuss, however, none of these theories comfortably fits with the language of

Section 2, much less with the basic "congressional desire to enforce agreements into which the parties had entered." *Volt Info. Sciences, Inc. v. Board of Trustees*, 489 U.S. 468, 478 (1989) (quoting *Dean Witter Reynolds, Inc. v. Byrd*, 470 U.S. 213, 220 (1985).

I. THE COURT SHOULD NOT OVERRULE *SOUTHLAND CORP v. KEATING.*

Although Alabama and other States (supported by respondents) urge this Court to overrule *Southland Corp. v. Keating*, and thus allow state courts to employ doctrines inimical to arbitration agreements, Ala. Br. at 1-20; Resp. Br. at 12-14, they offer nothing approaching a sufficient reason to do so. "Time and time again, this Court has recognized that 'the doctrine of *stare decisis* is of fundamental importance to the rule of law.'" *Hilton v. South Carolina Pub. Rys. Comm'n*, 112 S. Ct. 560, 563 (1991) (quoting *Welch v. Texas Dep't of Highways*, 483 U.S. 468, 494 (1987)). Noting that "[a]dherence to precedent promotes stability, predictability, and respect for judicial authority," 112 S. Ct. at 564, the Court has said that it "will not depart from the doctrine of *stare decisis* without some compelling justification." *Ibid.* The Court has further emphasized that "'[c]onsiderations of *stare decisis* have special force in the area of statutory interpretation, for here, unlike in the context of constitutional interpretation, the legislative power is implicated, and Congress remains free to alter what we have done.'" *Ibid.* (quoting *Patterson v. McLean Credit Union*, 491 U.S. 164, 172-73 (1989)). And, "[c]onsiderations in favor of *stare decisis* are at their acme in cases involving property and contract rights, where reliance interests are involved . . . ." *Payne v. Tennessee*, 111 S. Ct. 2597, 2610 (1991).

There is no "compelling justification" for departing from *stare decisis* here. To begin with, the States have given no reason why they waited 10 years—during which time thousands upon thousands of arbitration agreements

have been formed on the basis of existing law—to come forward with this point. Although they contend that they had no notice of the presence of this issue in *Southland Corp.*, saying that "the questions presented in *Southland* did not explicitly identify the Act's application to state court as the issue to be decided by this Court" (Ala. Br. at 2), they can hardly deny that the issue was necessarily present in a case involving enforcement of an arbitration agreement in state court. Moreover, they offer no explanation for their silence in *Perry v. Thomas* or *Volt Info. Sciences*, decided seven and five years ago respectively, both of which likewise involved issues about enforcement of arbitration agreements in state court. At the very least, therefore, the decision now to address the issue decided in *Southland Corp.* is highly belated.

The States (and respondents) also have little new to contribute. Having said that the Court in *Southland Corp.* "was denied the benefit of adversarial briefing on the matter" (Ala. Br. at 1), the States simply submit that "Justice O'Connor's dissent in *Southland* . . . is demonstrably correct and should be adopted by this Court as the proper interpretation of the FAA." Ala. Br. at 2. This suggestion seems little more than a plea to overrule a prior considered decision on the basis of a change in composition of the Court. The doctrine of *stare decisis* itself, however, reflects the principle that existing law should not commonly be set aside simply to reflect changes in the membership of the Court. *See, e.g., Florida Dep't of Health & Rehabilitative Servs. v. Florida Nursing Home Ass'n*, 450 U.S. 147, 153 (1981) (Stevens, J., concurring); *Mapp v. Ohio*, 367 U.S. 643, 677 (1961) (Harlan, J., dissenting).

Nor have events since the decision in *Southland Corp.* cast doubt upon its basic premises. Although the States say that the decision in *Volt Info. Sciences* has "undercut" *Southland Corp.*, Ala. Br. at 3, that is wishful thinking on their part. The Court in *Volt* did not question

that state courts have an obligation, under Section 2, to enforce arbitration agreements according to their terms: it simply made clear that, as part of those terms, the contracting parties could agree to be bound by certain provisions of state law. Given that "the federal policy is simply to ensure the enforceability, according to their terms, of private agreements to arbitrate" (489 U.S. at 476), and given that "parties are generally free to structure their arbitration agreements as they see fit" (*id.* at 479), the Court merely recognized that courts—whether state or federal—should ordinarily give effect to the parties' own intentions about how to arbitrate their claims. Nothing in that decision states, or even implies, that state courts should be free to do the opposite: disregard the stated agreement of the parties on the basis of legislative or judicial hostility towards agreements to arbitrate.

Finally, the States argue that Section 2 (as construed in *Southland Corp.*) infringes upon their sovereign rights to regulate contracts and protect consumers and that it lacks a clear enough statement of congressional intent to do so. Ala. Br. at 8-9. But this argument has a number of flaws. First of all, if the States mean to say that Section 2 fails to preempt state laws hostile to arbitration, then it would follow that Section 2 is inapplicable even in *federal* court, at least when state law typically provides the substantive law. As a general rule, the power of states to regulate contracts does not come and go depending on the forum in which suit is brought, yet the States make no attempt to explain why their theory leaves off at state courts. Moreover, and in any event, their argument against preemption of anti-arbitration laws is foreclosed by the fact that Congress *did* make a clear statement with respect to enforcement of arbitration agreements: those agreements are "valid, irrevocable, and enforceable" to the same extent as other contracts. And, by specifically providing that contracts to arbitrate could be held invalid "upon such grounds as exist at law or in equity for the revocation of any contract," 9 U.S.C. § 2, Congress left

little room for States to argue, as they do here, that Section 2 also allows for revocation of arbitration agreements based on nothing more than a dislike of arbitration agreements generally.

II. THE SCOPE OF SECTION 2 DOES NOT DEPEND UPON THE PARTIES' AGREEMENT ABOUT THE EXTENT OF INTERSTATE COMMERCE INVOLVED IN THEIR TRANSACTION.

To provide context for the arguments made by respondents and their *amici curiae* with respect to the scope of Section 2, it is worth setting out what they do not contest. First, despite some grumbling, they do not dispute that respondents entered into a written agreement to arbitrate disputes arising out of the termite protection plan with petitioners. Resp. Br. at 2-3. Furthermore, they do not dispute that, were it not for the specific Alabama policy disfavoring arbitration agreements, this agreement would be fully binding as a matter of state law: that is, nothing in the agreement would be grounds for revocation of *any* contract under state law. Nor do they deny that the materials used to treat respondents' home—the principal obligation undertaken by petitioners pursuant to the contract —moved in interstate commerce. *Id.* at 7. And they necessarily accept that Congress has the power to make the arbitration agreement "valid, irrevocable, and enforceable" as a matter of substantive federal law.

Respondents nevertheless urge a reading of Section 2 that would allow them to walk away from their agreement to arbitrate (while continuing to press their claims for damages under the same contract), giving full play to state law disfavoring agreements to arbitrate. The linchpin of this argument is that the words "a contract evidencing a transaction involving commerce" require that the contract explicitly reflect the interstate elements of the transaction (and, thus, demonstrate the "contemplation" by the parties of "substantial interstate activity"). *See* Resp. Br. at 15-20. But this reading, while perhaps not unimaginable, is certainly unnatural. Given that the words

"transaction involving commerce" (like the words "maritime transaction") are plainly intended to mark out the jurisdictional bounds of the statute, it would be extremely odd to have made the presence or absence of jurisdiction turn on the parties' understanding about the jurisdictional facts, rather than on the facts themselves. Reading the words together, therefore, it seems most natural to think that Congress imposed two related, but distinct, requirements: to establish a jurisdictional nexus, there must be a "transaction involving interstate commerce" and, to assure that the agreement to arbitrate relates to that transaction, there must be a contract (containing a written agreement to arbitrate) "evidencing" the transaction. Those conditions having been satisfied, it is difficult to understand what difference it should make that the parties do or do not set forth the interstate elements of the transaction in the contract.

Respondents attempt to address this point by saying that the Act is intended to carry out the "expectations" of the parties. Resp. Br. at 17. But, here, respondents are mixing apples and oranges. It is correct, indeed fundamental, to say that the Act seeks to advance the parties' "expectations" *about arbitration*, but that is very different from saying that the scope of the Act turns on the parties' "contemplation" *about interstate commerce*. Thus, while this Court has repeatedly recognized that Section 2 comes into play only after contracting parties have agreed to submit disputes to arbitration, *see, e.g., Volt Info. Sciences*, 489 U.S. at 476, it has never suggested that the parties must also agree about the extent of interstate commerce involved in their transaction. Provided that the agreement to arbitrate exists, as it does here, Section 2 operates to make that agreement enforceable so long as the necessary jurisdictional grounds (a "maritime transaction" or "a transaction involving commerce") have been met.

Respondents' argument would be more compelling, of course, if there were some basis to think that the parties'

expectations about arbitration were tied to their expectations about interstate commerce. But respondents do not put forward any such argument, and for good reason. To adopt that theory, it would be necessary to believe that parties enter into written agreements to arbitrate while secretly anticipating that (for want of adequate interstate activity) state law will be deemed to apply and make their agreement effectively meaningless. Quite apart from the fact that this speculation is implausible, it supposes a roundabout, if not actively deceitful, way of evading arbitration, and it is hardly likely that Congress meant to encourage it. Thus, insofar as a meeting of the minds is concerned, it is only the agreement to arbitrate, not an agreement about interstate commerce, that the Act requires.[1]

The reasoning employed by Judge Lumbard, heavily relied on by respondents (*see* Resp. Br. at 15-19), is similarly unpersuasive. Rejecting the view (adopted by the Second Circuit in an earlier case) that "Congress intended to use to the fullest possible extent its powers to regulate commerce as it was affected by arbitration agreements," *Metro Indus. Painting Corp. v. Terminal Constr. Co.*, 287 F.2d 382, 386 (2d Cir.), *cert. denied*, 368 U.S. 817 (1961), Judge Lumbard instead concluded that "we must be cautious in construing the act lest we excessively encroach on the powers which Congressional policy, if not the Constitution, would reserve to the states." *Ibid.* But this "cautio[n]" leads Judge Lumbard to the same error that respondents make: in deliberately seeking grounds to narrow the reach of the Act, he mixes together the understanding of the parties regarding arbitration with their understanding regarding interstate commerce to pro-

[1] We note that the origin of the language "contract evidencing a transaction involving commerce" fully supports the notion that Congress was tailoring the Act to the extent of its legislative powers. *See* Pet. Br. 15-16. Neither respondents nor their *amici curiae* have any response to this point.

duce a limitation not reasonably derived from the statute.[2] Thus, while he is entirely correct in saying that Congress did not intend to impose arbitration on those who had not agreed to it, he is incorrect in deciding that those who have agreed to it—and done so in contracts dealing with transactions involving interstate commerce in fact—may be permitted to avoid their obligations based on later claims that they did not "contemplate" the interstate activity involved.

We submit, therefore, that the "contemplation-of-the-parties" test has no place in the application of Section 2, even if that section were to be construed without any regard for the policies underlying the Act. But we note that respondents make no effort to explain why, even though "questions of arbitrability must be addressed with a healthy regard for the federal policy favoring arbitration" (*Gilmer*, 111 S. Ct. at 1652 (internal quotes omitted)), questions about the scope of Section 2 should not. If anything, it would seem that federal policy should play a *greater* role in construction of the *Act*, which reflects the intent of Congress itself, than in construction of arbitration agreements, which reflect the intent of the contracting parties. And, given that Congress had, as its primary intention, to make voluntary agreements enforceable, it is sensible to think that Congress would wish to apply that policy fully throughout the fields that it marked out.

The "contemplation-of-the-parties" test also seems to raise more problems than it solves. Described by respondents as "largely objective" (Resp. Br. at 21), and by one *amicus curiae* as "objective, not subjective" (SPLC Br. at 7), the test is, in fact, mostly unfathomable. As an initial matter, it invites a cumbersome inquiry into the

[2] Indeed, Judge Lumbard ultimately works backwards in construing the statute, saying that "[t]he rule of construction should be based on some more realistic appraisal of the ends Congress wished to serve." 287 F.2d at 387.

subjective understandings of the parties about the nature of the transaction and any interstate activity likely associated with it. Although the contract itself would be evidence of the parties' "contemplation," there is no obvious basis for limiting the inquiry to the contract rather than allowing either party to argue that it does not fully reflect the understood nature of the transaction. Moreover, in the case of contracts assumed by successor parties (like the one involved here), the inquiry would be further complicated by the need to examine the understandings of the *original* parties, unless a previously binding agreement were to become voidable simply because the successors (or, perhaps, one successor) to the contract did not also "contemplate" substantial interstate activity. With so much ambiguity unresolved, the test seems especially prone to case-by-case manipulation in the hands of courts wishing to avoid the federal directive to enforce arbitration agreements.

Finally, citing a handful of cases, respondents make the argument that "[t]he 'contemplation of the parties' test is also perfectly consistent with Congress' understanding of background Commerce Clause jurisprudence when the Act was passed in 1925." Resp. Br. at 22. But the cases are not at all on point,[3] and, anyway, there is no indica-

[3] Two of the cited cases—*Cincinnati, Portsmouth, Big Sandy, & Pomeroy Packet Co. v. Bay*, 200 U.S. 179 (1906) and *Binderup v. Pathe Exchange, Inc.*, 263 U.S. 291 (1923)—involve combinations or conspiracies to restrain interstate commerce under the Sherman Act. This Court had observed at the time that, to demonstrate an unlawful conspiracy or combination, *"the intent to injure, obstruct, or restrain interstate commerce* must appear as an obvious consequence of what is to be done, or be shown by direct evidence or other circumstances." *United Mine Workers v. Coronado Coal Co.*, 259 U.S. 344, 408 (1922) (emphasis added). Even respondents do not contend that the FAA incorporates any such standard. The third case—*Kansas City Structural Steel Co. v. Arkansas*, 269 U.S. 148 (1925)—though noting that local transactions were "contemplated," was decided, not on that basis, but on the basis of *actual* local activities. *See id.* at 152 ("the things *done* by the plaintiff in error in Arkansas . . . constitute or include intrastate business") (emphasis added).

tion that Congress had them in mind at the time. In contrast, a brief submitted as part of the legislative record explicitly informed Congress that its powers over interstate commerce "govern every agency or act which bears so close a relationship to interstate commerce that they can reasonably be said to affect it" and that "[c]ontracts relating to interstate commerce are within the regulatory powers of Congress." *See* Joint Hearings on S. 1005 and H.R. 646 Before the Subcomm. of the Comms. on the Judiciary, 68th Cong., 1st Sess. 38 (1924) (Brief submitted by Julius H. Cohen, member of the Committee on Commerce, Trade & Commercial Law of the ABA and the General Counsel for the N.Y. State Chamber of Commerce). In light of the fact that the relevant House Report tracks this language ("contracts relating to interstate commerce") in describing the scope of the commerce power, H.R. Rep. No. 96, 68th Cong., 1st Sess. 1 (1924), it is fanciful to attribute to Congress an intent to rely on the "contemplation" of the parties in setting the jurisdictional bounds of the Act.

III. THE "FLOW" OR "CURRENT" OF INTERSTATE COMMERCE TEST SHOULD NOT BE READ INTO SECTION 2.

Respondents argue that, in any event, Congress did not intend to use its commerce powers to the fullest, but rather meant to reach only transactions by merchants in the "flow" or "current" of interstate commerce. This Court, of course, has said just the opposite. *See Perry*, 482 U.S. at 490 (Act "embodies Congress' intent to provide for the enforcement of arbitration agreements within the full reach of the Commerce Clause"). While that statement is not controlling, it does reflect an understanding of the Act reached by a number of other courts. *See, e.g., Foster v. Turley*, 808 F.2d 38 (10th Cir. 1986); *Robert Lawrence Co. v. Devonshire Fabrics, Inc.*, 271

F.2d 402, 407 (2d Cir. 1959), *cert. granted*, 362 U.S. 909, *cert. dismissed*, 364 U.S. 801 (1960). Respondents' efforts to disprove it are singularly unimpressive.

The principal argument advanced by respondents is that, to validate the statement in *Perry*, the Court would have to overrule *Bernhardt v. Polygraphic Co. of America*, 350 U.S. 198 (1956). Resp. Br. at 11, 20. But, in taking that position, respondents utterly ignore the test actually employed by this Court in *Bernhardt*: whether "[the employee] while performing his duties under the employment contract was working 'in' commerce, was producing goods for commerce, or *was engaging in activity that affected commerce*, within the meaning of our decisions." 350 U.S. at 200-01 (emphasis added). The last part of that test plainly reflects the broad extent of powers granted to Congress under the Commerce Clause, without limiting the inquiry to the "flow" or "current" of interstate commerce. While one can fairly question whether the facts of the case fell within or without this test, it is totally off-the-mark to say that *Bernhardt* established that, in enacting Section 2, Congress called upon only a fraction of its powers under the Commerce Clause.

Respondents then submit that "the phrase 'a transaction involving commerce' should be defined to mean a transaction between businesspersons who are part of the 'flowing stream' of commerce as the term 'commerce' was understood in 1925." Resp. Br. at 26. But this Court has already rejected the argument that Section 2 applies only to dealings between merchants. *See Prima Paint*, 388 U.S. at 401 n.7. Moreover, businesspersons aside, it is simply mistaken to assert that, in 1925, the power of Congress to regulate interstate commerce was limited to "a flowing stream from one State to another formed by a regular course of business." Resp. Br. at 26. As one case cited by respondents itself makes clear, "if Congress deems certain recurring practices though not really part of interstate commerce, likely to obstruct, restrain, or burden it, it has the power to subject them to national supervision

and restraint." *United Mine Workers v. Coronado Coal Co.*, 259 U.S. 344, 408 (1922). That view, as we have already noted, corresponds closely to the contemporaneous views put before Congress regarding the extent of its powers to regulate commerce. *See* page 11 *supra*.

The existence of a power to regulate, of course, is not conclusive on the question whether Congress exercised it. Respondents and their *amici curiae*, however, have offered little reason to suppose that Congress did not. One *amicus curiae* argues that, in the absence of a narrowing construction, "[f]ederal law would . . . guarantee landlords, television repair shops, dry cleaners, and every other local business the right—regardless of their highly attenuated connection to interstate commerce—to insert clauses into their form contracts waiving consumers' rights to a judicial forum." SPLC Br. at 3. But, quite apart from the threshold requirement of a written agreement to arbitrate—thus eliminating most casual consumer transactions—it is well recognized that a "highly attenuated connection to interstate commerce" is not enough to fall within the boundaries of the Commerce Clause. To the contrary, the Court has recognized that the exercise of the commerce power cannot be extended to "effects upon interstate commerce so indirect and remote" (*NLRB v. Jones & Laughlin Steel Co.*, 301 U.S. 1, 37 (1937)) that the distinction between local and national activities would be lost. Where the nexus is more substantial, however, we see no reason why parties should not be able to make binding agreements to arbitrate disputes about the purchase of television sets or the sale of services to local consumers.[4]

[4] The service purchased here, in a written contract between parties in different States, involved the direct application of materials brought into Alabama from out-of-state in order to perform that service. Such transactions, like the direct sales of goods moving in interstate commerce, seem well within the outer boundaries of those commercial dealings that, taken in the aggregate, have a substantial effect on interstate commerce. *See, e.g., Fry v. United*

The attempts by respondents and their *amici curiae* to narrow Section 2 appears to reflect a concern that consumers lack the bargaining power to resist agreements to arbitrate. Resp. Br. at 11-12; Ala. Br. at 19; SPLC Br. at 12. That this is so is certainly not a foregone conclusion: neither respondents nor their *amici curiae* have demonstrated that consumers willing to pay higher costs for a product or service cannot bargain to eliminate any agreement to arbitrate. But, in any case, this Court has repeatedly rejected arguments that Section 2 does not apply to persons of unequal bargaining power. *See Gilmer*, 111 S. Ct. at 1655-56; *Mitsubishi Motors*, 473 U.S. at 627. The proper question, as the Court has made clear, is not whether the parties have different levels of bargaining power but whether any inequality is "grounds . . . for the revocation of any contract." 9 U.S.C. § 2. If the inequality of bargaining power is not enough to invalidate other obligations, then a state hostile to arbitration may not single it out as a basis for voiding an agreement to arbitrate. Thus, while a State retains full power to protect its citizens against adhesion contracts, it may not establish special, discriminatory standards disfavoring arbitration agreements. Section 2 puts contracts to arbitrate "upon the same footing as other contracts," *Scherk v. Alberto-Culver Co.*, 417 U.S. 506, 511 (1974), no more and no less.

States, 421 U.S. 542, 547 (1975); *Perez v. United States*, 402 U.S. 146, 154 (1971).

CONCLUSION

The judgment of the Supreme Court of Alabama should be reversed.

Respectfully submitted,

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IN THE

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OCTOBER TERM, 1993

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Petitioners,

—v.—

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STEVEN GWIN and JAN GWIN,

Respondents.

ON WRIT OF CERTIORARI TO THE
SUPREME COURT OF ALABAMA

MOTION FOR LEAVE TO FILE BRIEF AS *AMICUS CURIAE* AND BRIEF OF AMERICAN ARBITRATION ASSOCIATION AS *AMICUS CURIAE* IN SUPPORT OF PETITIONERS

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ON WRIT OF CERTIORARI TO THE SUPREME COURT OF ALABAMA

MOTION FOR LEAVE TO FILE BRIEF AS *AMICUS CURIAE*

Pursuant to Rule 37.4 of the Rules of this Court, the American Arbitration Association ("AAA" or the "Association") hereby respectfully moves for leave to file the annexed brief as *amicus curiae*. Petitioners' written consent to such filing has been obtained. The consent of Respondents was requested but refused.

The AAA is an educational, membership organization incorporated in 1926 and operating under the Not-for-Profit Corporation Law of the State of New York. The Association is dedicated to the dissemination of knowledge throughout the United States and other countries regarding arbitration and other alternative mechanisms for resolving disputes. The AAA does not act as an arbitrator of disputes; rather, it provides impartial rules,

procedures, and administrative assistance to parties desiring to use its neutral facilities.

This case raises an issue that has long occupied state and lower federal courts in the United States—the scope of applicability of the Federal Arbitration Act, 9 U.S.C. §§ 1-16. The issue is particularly important with respect to controversies arising in states, such as Alabama in the present case, that view arbitration with suspicion. As the leading arbitration institution in the United States, the AAA promotes arbitration as a relatively speedy, efficient, and inexpensive method of resolving disputes. Litigation about litigation, or about litigation versus arbitration, is inconsistent with the promise of arbitration and with the efforts of the Association. The AAA accordingly has a strong interest in seeing that uncertainty about the reach of the Federal Arbitration Act is removed, so that parties to a dispute can know whether or not they are required to arbitrate, and so that parties who desire to have their contracts subject to arbitration can know what type of provisions to include in their contracts.

The AAA has no interest in the outcome of the underlying dispute between the home owner and the termite protection company. The arbitration clause at issue, however, was based on the standard clause contained in the Commercial Arbitration Rules pamphlet published by the AAA. The Association views with concern any possibility that this Court might change direction from its strong support of arbitration over the past two decades, regardless of whether the arbitration in any particular case is to be administered by the AAA, as here, or by another organization, as in three of the four previous cases in which the AAA has filed a brief as *amicus curiae*. *See Shearson/American Express, Inc. v. McMahon*, 482 U.S. 220 (1987) (National Association of Securities Dealers); *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614 (1985) (Japan Commercial Arbitration Association); *Scherk v. Alberto-Culver Co.*, 417 U.S. 506 (1974) (International Chamber of Commerce); *Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, 388 U.S. 395 (1967) (AAA).

The AAA is uniquely in a position to offer information gathered in the course of its extensive experience in the administration of arbitration. In addition, the AAA is able to bring its perspective to the broader issues concerning the direction of the development of federal arbitration law by this Court and by Congress. Petitioners did not extensively address these issues in their petition for certiorari, and the AAA has no reason to believe that they will do so in their brief on the merits.

WHEREFORE the American Arbitration Association respectfully moves this Court for leave to file the annexed brief as *amicus curiae* in support of petitioner.

Respectfully submitted,

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BRIEF OF AMERICAN ARBITRATION ASSOCIATION AS *AMICUS CURIAE* IN SUPPORT OF PETITIONERS

INTEREST OF AMICUS

The interest of *amicus curiae* American Arbitration Association ("AAA" or the "Association") is set forth in the motion for leave to file this brief, which is bound herewith pursuant to Rule 37.4 of this Court.

SUMMARY OF ARGUMENT

This Court has issued rulings in favor of arbitration in an unbroken series of cases for more than a quarter century. Only a major shift in direction for the Court could sustain the decision below.

This Court's prior decisions, the plain words of the Arbitration Act and the legislative history of that Act indicate that Congress intended to extend the Act to the full reach of its powers

to regulate interstate and foreign commerce. More recently, Congress has repeatedly reconfirmed its support for arbitration as a means of dispute settlement in commercial disputes. Apart from hostility to arbitration, which this Court has decisively rejected, the Alabama Supreme Court's construction of the Act has no discernible basis in history or logic.

The evidence is overwhelming that arbitration is fair and efficient. Arbitration not only relieves overcrowded courts of unnecessary burdens but it provides resolution of disputes without distorting justice.

The standard applied by the Alabama Supreme Court in the present case to measure the scope of the Federal Arbitration Act invites pre-arbitration litigation about disputes. The only way to give effect to the congressional intent to allow parties to choose arbitration as a speedy and economical means of resolving disputes is to make clear that the reach of the Arbitration Act is coextensive with the powers of Congress under the Commerce Clause.

ARGUMENT

I.

Since 1967 This Court Has Consistently Rejected All Attempts To Restrict Enforcement of Agreements To Arbitrate.

Beginning in 1967, this Court has consistently upheld agreements to arbitrate. In an unbroken series of decisions since that time, this Court has repudiated the ambivalence to arbitration that it displayed forty years ago in *Wilko v. Swan*, 346 U.S. 427 (1953). In *Wilko*, the Court invalidated an agreement to arbitrate in a contract between a securities brokerage firm and its customer, essentially on the ground that arbitration could not assure to the customer the kind of protection granted to investors by the Securities Act of 1933, 15 U.S.C. §§ 77a–77aa. Not only has this Court expressly overruled *Wilko* in *Rodriguez de Quijas v. Shearson/American Express, Inc.*, 490 U.S. 477 (1989), but it has

consistently stressed that arbitration is a fair system of dispute resolution, that arbitrators are equipped to decide complex as well as simple controversies, that they can be authorized to pass on statutory as well as common-law claims, and that if there is a question about the validity of a contract containing an agreement to arbitrate, that question is to be decided by the arbitrators.

First, this court has, in a series of cases, made clear that any doubts concerning the scope of arbitrable issues should be resolved in favor of arbitration. In *Prima Paint Corp. v. Flood & Conklin Manufacturing Co.*, 388 U.S. 395 (1967), this Court held that a challenge to the validity of a contract containing an arbitration clause was a question for the arbitrators, not the court, and rejected the argument that the arbitrators would be without jurisdiction without a valid contract. Any other decision would have seriously diminished the value of arbitration by requiring essentially two trials: litigation in court about contract validity, followed by arbitration about breach and damages. In deciding as it did, the Court stated that

> we not only honor the plain meaning of the statute but also the unmistakably clear congressional purpose that the arbitration procedure, when selected by the parties to a contract, be speedy and not subject to delay and obstruction in the courts.

388 U.S. at 404.

This Court extended the reasoning of *Prima Paint* in *Moses H. Cone Memorial Hospital v. Mercury Construction Corp.*, 460 U.S. 1 (1983), in which one party asserted that the other party had waived its right to arbitrate. The Court rejected the application of a state-law waiver standard and held that

> Section 2 is a congressional declaration of a liberal federal policy favoring arbitration agreements, notwithstanding any state substantive or procedural policies to the contrary. . . . The Arbitration Act establishes that, as a

> matter of federal law, any doubts concerning the scope of arbitrable issues should be resolved in favor of arbitration.

460 U.S. at 24-25.

Second, this Court in *Southland Corp. v. Keating*, 465 U.S. 1 (1984), confirmed what it had already stated in *Moses H. Cone*, that the Arbitration Act is federal substantive law applicable in state as well as federal court. In *Southland*, this Court reversed the Supreme Court of California's holding that claims based on that state's franchise law were excluded from coverage under an agreement to arbitrate. Chief Justice Burger wrote for the Court:

> Contracts to arbitrate are not to be avoided by allowing one party to ignore the contract and resort to the courts. Such a course could lead to prolonged litigation, one of the very risks the parties, by contracting for arbitration, sought to eliminate. . . . In enacting § 2 of the federal Act, Congress declared a national policy favoring arbitration and withdrew the power of the states to require a judicial forum for the resolution of claims which the contracting parties agreed to resolve by arbitration.

465 U.S. at 7, 10.

Southland was followed by *Perry v. Thomas*, 482 U.S. 483 (1987), in which the Court reiterated its holding that a state law withdrawing certain claims from arbitration must give way to the federal policy favoring arbitration. Of particular relevance to the present case, Justice Marshall wrote for the Court that a state court "may not . . . in assessing the rights of litigants to enforce an arbitration agreement, construe that agreement in a manner different from that in which it otherwise construes nonarbitration agreements under state law." 482 U.S. at 492 n.9.

Third, this Court has made clear that it will not read implied exceptions into the broad coverage of the Arbitration Act. In *Scherk v. Alberto-Culver Co.*, 417 U.S. 506 (1974), the Court had to confront the question whether the rule of *Wilko v. Swan*, barring arbitration claims under the securities laws (or at least

under the Securities Act of 1933) applied to a securities-law claim arising out of an international transaction. This Court upheld the agreement to arbitrate in Paris:

> The invalidation of such an agreement in the case before us would not only allow the respondent to repudiate its solemn promise but would as well, reflect a "parochial concept that all disputes must be resolved under our laws and in our courts."

417 U.S. at 519 (quoting *The Bremen v. Zapata Off-Shore Co.*, 407 U.S. 1, 9 (1972)).

In *Dean Witter Reynolds, Inc. v. Byrd*, 470 U.S. 213 (1985), the Court was faced with the "intertwining" of arbitrable state law claims and claims under the Securities Act of 1933, then believed nonarbitrable. The Court of Appeals for the Ninth Circuit had held that since the federal claims were not arbitrable, the state law claims should not be arbitrated either. Again, the question was not free from doubt, but again this Court made the pro-arbitration decision, ordering that the arbitrable claims be arbitrated without delay even if some duplication of work resulted. Justice Marshall wrote for the Court:

> The preeminent concern of Congress in passing the [Arbitration] Act was to enforce private agreements into which parties had entered, and that concern requires that we rigorously enforce agreements to arbitrate, even if the result is "piecemeal" litigation, at least absent a countervailing policy manifested in another federal statute. . . . By compelling arbitration of state-law claims, a district court successfully protects the contractual rights of the parties and their rights under the Arbitration Act.

470 U.S. at 221.

In *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614 (1985), this Court again refused to exclude a class of cases from the reach of the Arbitration Act. *Mitsubishi* concerned a controversy between a Japanese manufacturer and an

automobile dealer in Puerto Rico that raised counterclaims under United States antitrust laws and a Puerto Rico dealers' protection statute. The Court of Appeals for the First Circuit held the antitrust claims nonarbitrable and separated them from the other claims and counterclaims. Notwithstanding support for that position by the State and Justice Departments, this Court reversed, holding that all claims must be submitted to arbitration under an agreement that called for arbitration in Tokyo under auspices of the Japan Commercial Arbitration Association and for application of Swiss law. Building on *Prima Paint*, *Scherk*, *Moses H. Cone*, and *Southland*, Justice Blackmun wrote for the Court:

> [W]e are well past the time when judicial suspicion of the desirability of arbitration and of the competence of arbitral tribunals inhibited the development of arbitration as an alternative means of dispute resolution. . . . Having made the bargain to arbitrate, the party should be held to it unless Congress itself has evinced an intention to preclude a waiver of judicial remedies. . . .

473 U.S. at 626-628.

Thereafter in *Shearson/American Express, Inc. v. McMahon*, 482 U.S. 220 (1987), and *Rodriguez de Quijas v. Shearson/American Express, Inc.*, 490 U.S. 477 (1989), the Court cleared up the remaining doubt about the arbitrability of securities claims, expressly holding that claims under the Securities Exchange Act of 1934, 15 U.S.C. §§ 78a-78*ll*, were not excluded from the scope of the Federal Arbitration Act, that RICO claims were not exempt from the Act, and finally that claims under the Securities Act of 1933 were not exempt and that *Wilko v. Swan* was expressly overruled. As the Court said in *McMahon*,

> [T]he mistrust of arbitration that formed the basis for the *Wilko* opinion in 1953 is difficult to square with the assessment of arbitration that has prevailed since that time.

482 U.S. at 233. *See also Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S. 20 (1991) (enforcing agreement to arbitrate claim

under Age Discrimination in Employment Act, 29 U.S.C. §§ 621-634).

In sum, this Court has rejected—not once but repeatedly—what Judge Jerome Frank called "the old judicial hostility to arbitration." *Kulukundis Shipping Co. v. Amtorg Trading Corp.*, 126 F.2d 978, 985 (2d Cir. 1942). The Court has heard all the arguments against enforcing agreements to arbitrate and has rejected all of them. The present case reflects a last pocket of resistance based on an unsound construction of the Arbitration Act. There is no reason for the Court to change its course in this case, and every reason to maintain its "healthy regard for the federal policy favoring arbitration." *Moses H. Cone*, 460 U.S. at 24.

II.

The Arbitration Act Extends to the Limits of the Powers of Congress under the Commerce Clause.

There can be no serious doubt today that the transaction at issue here—a service contract between a resident of Alabama and a company incorporated and having its principal place of business in another state, operating a termite-control business that extends throughout the United States, and using pesticides that have been transported in from several different states—is within Congress's power to regulate under the Commerce Clause. *See, e.g., Heart of Atlanta Motel v. United States*, 379 U.S. 241 (1964); *United States v. Sullivan*, 332 U.S. 689, 697-98 (1948); *Wickard v. Filburn*, 317 U.S. 111 (1942); *see also Barrett v. United States*, 423 U.S. 212 (1976). Indeed, neither the Supreme Court of Alabama nor, as we understand it, the Respondents in this case, contend that applying the Federal Arbitration Act to the present case would be unconstitutional.[1] The question, rather, is whether

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[1] The statement in *Bernhardt v. Polygraphic Company of America*, 350 U.S. 198 (1956), that the petitioner in that case—who entered into an employment contract that required him to relocate his residence across state lines—was not

(continued...)

the "commerce" provision of the Arbitration Act—like that of most statutes regulating interstate commerce—requires only that the transaction have an effect on commerce, or whether there is a "distinct standard unique to the application of the FAA." *Ex parte Warren*, 548 So. 2d 157, 160 (Ala.), *cert. denied*, 493 U.S. 998 (1989).

There is no basis in the prior decisions of this Court construing the Arbitration Act, in the language or legislative history of the Act, or in the Court's construction of other pre-New Deal legislation to support the artificially narrow construction that the Alabama Supreme Court has given the Act. All these sources make clear that the Act operates to the full reach of Congress's commerce power.

A. Congress Intended to Give the Broadest Possible Scope to the Arbitration Act.

This Court has already expressly stated that the Arbitration Act is

> a statute that embodies Congress' intent to provide for the enforcement of arbitration agreements within *the full reach of the Commerce Clause*.

Perry v. Thomas, 482 U.S. 483 at 490 (1987) (emphasis added). The legislative history of the Arbitration Act confirms that Congress intended to validate arbitration agreements to the full extent of its Commerce Clause powers. The congressional committee reports relating to the Arbitration Act, ch. 213, 43 Stat. 883 (1925), show no concern with the "local" or "national" character of the transactions governed by the Act, apart from a desire not to exceed the powers of Congress under the Constitution. The reports focus instead on Congress's disapproval of the

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[1](...continued)
"engaging in activity that affected commerce" is inconsistent with Congress's intent and with this Court's decision in *Prima Paint* and has been implicitly rejected in this Court's subsequent cases.

"anachronism of American law" by which courts at that time refused to specifically enforce arbitration agreements. H.R. Rep. No. 96, 68th Cong., 1st Sess. 1 (1924); S. Rep. No. 536, 68th Cong., 1st Sess. 2-3 (1924); *see also Southland*, 465 U.S. at 13 (discussing legislative history). As this Court summarized in *Perry v. Thomas*, the Arbitration Act's "general applicability reflects that '[t]he preeminent concern of Congress in passing the act was to enforce private agreements into which parties had entered. . . .' " 482 U.S. at 490 (quoting *Dean Witter Reynolds, Inc. v. Byrd*, 470 U.S. 213, 221 (1985)).

By adopting the Act in 1925, Congress sought to eradicate what even then was the "anachronism" of hostility to arbitration in all transactions within the field of its legislative competence.[2] The House Judiciary Committee concluded in its report that

> [t]he control over interstate commerce [one of the bases for the legislation] reaches not only the actual physical interstate shipment of goods but also contracts *relating to* interstate commerce.

H.R. Rep. No. 96, *supra*, at 1 (emphasis added), *quoted in Prima Paint Corp.*, 388 U.S. at 401 n.7. The brief of the American Manufacturers' Export Association of New York, submitted in support of the legislation to the House and Senate committees,

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[2] Julius Henry, who drafted the Arbitration Act bill for the American Bar Association, testified that the Act was the federal portion of a plan to "destroy the anachronism in the law" across the board; as he explained, "This is in three segments: The first is to get a State statute, and then to get a Federal law to cover interstate and foreign commerce and admiralty, and, third, to get a treaty with foreign countries." *Joint Hearings before the Subcommittees of the Committees on the Judiciary on S. 1005 and H.R. 646*, 68th Cong., 1st Sess. 16 (1924), *quoted in Prima Paint*, 388 U.S. at 405 n.13. Charles L. Bernstein of the New York Chamber of Commerce, another supporter of the bill, explained that the proposed legislation "follows the lines of the New York arbitration law, applying it to the fields wherein there is Federal jurisdiction. These fields are in admiralty and in foreign and interstate commerce." *Hearing on S. 4213 and S. 4214 before the Subcommittee of the Senate Committee on the Judiciary*, 67th Cong., 4th Sess. 2 (1923), *quoted in id.*

reflects the same contemporaneous understanding that the Act reaches to the limit of Congress's Commerce Clause powers:

> It is not only the actual and physical interstate shipment of goods which is subject to the interstate commerce powers of the Federal Government, but these powers govern every agency or act which bears so close a relationship to interstate commerce that they can reasonably be said to *affect* it. Contracts *relating to* interstate commerce are within the regulatory powers of Congress.

Joint Hearings before the Subcommittees of the Committees on the Judiciary on S. 1005 and H.R. 646, 68th Cong., 1st Sess. 38 (1924) (emphasis added).

This Court was thus fully justified in holding in *Prima Paint* that the Arbitration Act is substantive federal law "based upon . . . the incontestable federal foundations of control over interstate commerce," 388 U.S. at 405, and in *Southland* that

> the "involving commerce" requirement in § 2 [is] not . . . an inexplicable limitation on the power of the federal courts, but . . . a *necessary* qualification on a statute intended to apply in state and federal courts.

465 U.S. at 14-15 (emphasis added); *see also Moses H. Cone Memorial Hospital v. Mercury Construction Corp.*, 460 U.S. 1, 24-25 (1983).

B. There Is No Reason To Apply a Different Standard to the Arbitration Act Than to Other Acts of Congress Enacted Pursuant to the Commerce Power.

The contention in support of the decision of the Alabama Court's decision is essentially that

> the standard here applicable is not the "regulating standard" of "affecting interstate commerce", rather, the test for determining whether the transaction involves interstate

> commerce is a distinct standard unique to the application of the FAA.

Ex parte Warren, 548 So. 2d 157, 160 (Ala.), *cert. denied*, 493 U.S. 998 (1989). Once "the outmoded presumption of disfavoring arbitration proceedings" is rejected, however, *Rodriguez de Quijas*, 490 U.S. at 481, there is no reason to adopt a "distinct standard unique to . . . the FAA," *Ex parte Warren*, 548 So. 2d at 160.

In fact, the Alabama Supreme Court itself has stated that its long-standing hostility to arbitration has motivated its adoption of the "contemplated substantial interstate activity" test.[3] In explaining why it has preferred that test, which it had adopted in *Ex parte Warren*, instead of a "slightest nexus with interstate commerce" test, the Alabama Supreme Court has explained: "The standard in *Warren* better promotes our strong public policy *against* the use of predispute arbitration agreements." *Lopez v. Home Buyers Warranty Corp.*, 628 So. 2d 361, 363 n.2 (Ala. 1993) (emphasis added), *petition for cert. filed*, 62 U.S.L.W. 3430 (U.S. Dec. 22, 1993) (No. 93-995); *see also Old Republic Ins. Co. v. Lanier*, No. 1921387, 1994 Ala. LEXIS 276, *15, 1994 WL 154193, *5 (Ala. Apr. 29, 1994) ("To comport with our strong policy against arbitration, we must adopt a narrow standard for determining when the FAA applies . . .").[4]

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[3] Alabama's policy against arbitration, presently embodied in Ala. Code § 8-1-41(3) (1975) (providing that predispute arbitration agreements cannot be specifically enforced), has its roots in the jealousy with which English and American courts formerly viewed agreements to "oust the courts of their jurisdiction." *H. L. Fuller Constr. Co. v. Industrial Dev. Bd.*, 590 So. 2d 218, 221 (Ala. 1991). This hostility to arbitration seems to have first appeared in Alabama in *Bozeman v. Gilbert*, 1 Ala. 90 (1840), in which the Alabama Supreme Court refused to enforce an arbitration agreement in a case relating to an alleged breach of warranty in the sale of a jackass.

[4] The Alabama Supreme Court's antipathy toward arbitration agreements has come to this Court before. In *Ex parte Alabama Oxygen Co.*, 433 So. 2d 1158 (Ala. 1983), the Alabama Supreme Court rejected as dicta the statement in *Moses*

(continued...)

The interpretation of a federal statute is, however, a question of federal law. Apart from hostility to arbitration, which this Court has decisively rejected, there is no justification in history or logic for construing the words of the Arbitration Act as the Alabama Supreme Court has done. In exercising its powers over interstate commerce, Congress, legislating at different times and with different drafters, has used such words as "affecting" interstate commerce, as in the National Labor Relations Act, 29 U.S.C. § 160(a), or "involving" commerce, as in the Arbitration Act, 9 U.S.C. § 1, or has referred merely to the "use of any means or instrumentality of interstate commerce," as in the Securities Exchange Act, 15 U.S.C. § 78j, or to "restraint of trade or commerce among the several States," as in the Sherman Antitrust Act, 15 U.S.C. § 1.[5] While the interpretation of the commerce power has had its ups and downs since the groundbreaking decision in *Gibbons v. Ogden*, 22 U.S. (9 Wheat.) 1 (1824), it would be wholly arbitrary to assign different categories of application to different enactments of Congress on the basis of the

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[4](...continued)
Cone that the Arbitration Act applies in state courts, and refused to enforce an arbitration clause in a construction contract. After deciding *Southland Corp. v. Keating*, this court vacated the judgment in *Alabama Oxygen* and remanded the case for reconsideration. *York Int'l v. Alabama Oxygen Co.*, 465 U.S. 1016 (1984). On remand, the Alabama Supreme Court reversed its original decision as required by *Southland*. *Ex parte Alabama Oxygen Co.*, 452 So. 2d 860 (Ala. 1984). As the present case and other recent decisions of that court have shown, however, it has not abandoned its attempts to narrow the scope of the Arbitration Act in order to defeat agreements to arbitrate.

[5] Justice Black's statement, in his dissent in *Prima Paint*, 388 U.S. at 410, that "affect commerce" is "the statutory language Congress normally uses when it wishes to exercise its full powers over commerce," is therefore unpersuasive. The relevant language in both of the statutes that Justice Black cited as examples was enacted during the 1930s, a decade or more after the Arbitration Act was passed. *See* National Labor Relations Act, ch. 372, § 2, 49 Stat. 450 (1935) (codified as amended at 29 U.S.C. § 152); Act of Aug. 11, 1939, ch. 685, § 1, 53 Stat. 1404 (adding provision containing "affecting commerce" language to Federal Employers' Liability Act, codified as amended at 45 U.S.C. § 51).

particular words that Congress used to identify the constitutional limits of its commerce powers in any particular statute.

Even if Congress, when enacting the Arbitration Act, had not understood the extent of its Commerce Clause powers as does the Congress of today, there would be no reason to leave the scope of the Arbitration Act frozen as of 1925 in view of Congress's evident intent to extend the Arbitration Act to all transactions within its commerce power. Congress's explicit rejection of hostility to arbitration obviously did not stop at the edge of a pre-New Deal understanding of its Commerce Clause powers. As this Court's decisions have recognized, older federal statutes such as the Arbitration Act should not be subjected to now-discredited limitations on Congress's powers that prevailed when Congress enacted those statutes, but should be interpreted in view of modern, more expansive notions of those powers.

For example, this Court has expressly recognized that the Sherman Antitrust Act, 15 U.S.C. §§ 1-7, adopted in 1890, must be allowed to expand along with the Court's interpretation of the Commerce Clause. *E.g., McLain v. Real Estate Bd.*, 444 U.S. 232, 241 (1980); *Hospital Bldg. Co. v. Trustees of Rex Hosp.*, 425 U.S. 738, 743 n.2 (1976). Shortly before the Sherman Act was enacted, this Court had held that the regulation of manufacturing was not within Congress's commerce powers. *Kidd v. Pearson*, 128 U.S. 1 (1888). Soon after Congress enacted the Sherman Act, the Court held that a scheme to monopolize the manufacture of sugar was outside the reach of Congress's commerce powers and therefore not subject to the Sherman Act, even though the manufacturers sold the sugar in interstate commerce. *United States v. E.C. Knight Co.*, 156 U.S. 1 (1895). Nonetheless, after this Court in *United States v. Darby*, 312 U.S. 100, 113-117 (1941), had laid to rest the notion that Congress's commerce powers did not extend to the regulation of manufacturing, the Court had no difficulty in applying the Sherman Act to a scheme to monopolize sugar manufacture in *Mandeville Island Farms v. American Crystal Sugar Co.*, 334 U.S. 219, 229-31 (1948) (criticizing *E.C. Knight*).

There is no sound basis for imposing any greater restrictions on the Arbitration Act than on other Congressional enactments pertaining to interstate commerce. This Court should make clear that an agreement to arbitrate in any commercial transaction within the scope of Congress's commerce powers is within the scope of the Arbitration Act.

C. Congress has Repeatedly Adopted a Stance in Favor of the Expanded Use of Arbitration to Resolve Commercial Disputes.

Congress has shown in numerous ways that it concurs fully with the statement of this Court that "Section 2 [of the Arbitration Act] is a congressional declaration of a liberal federal policy favoring arbitration agreements, notwithstanding any state substantive or procedural policies to the contrary." *Moses H. Cone*, 460 U.S. at 24. Congress has made no effort to limit arbitration of commercial disputes, nor has it expressed any disapproval of the broad construction that this Court and other courts have given the first chapter of the Arbitration Act, 9 U.S.C. §§ 1-14, which remains essentially unchanged from 1925. Indeed, Congress has looked with favor on the trend toward widening the use of arbitration in commercial disputes and has participated in that trend in several areas.

In the international sphere, Congress has enacted legislation implementing the New York and Panama Conventions, designed to facilitate the enforcement of international arbitration agreements and awards. 9 U.S.C. §§ 201-208 (enacted 1970); *id.* §§ 301-306 (enacted 1990). Congress has also legislated to prevent foreign governments from invoking the "act of state" doctrine to avoid the enforcement of arbitration agreements and awards. 9 U.S.C. § 15 (enacted 1988).

Congress has endorsed the expanded use of arbitration in domestic transactions as well. For instance, when Congress established the Commodity Futures Trading Commission in 1974 to oversee registered futures associations, it required as one of the

conditions for registration and approval of such an association that its rules provide for a "fair and equitable procedure through arbitration or otherwise for the settlement of a customer's claims and grievances. . . ." Commodity Futures Trading Commission Act of 1974, Pub. L. No. 93-463, sec. 301, § 17(b)(10), 88 Stat. 1389, 1408-09 (adding § 17(b)(10) to the Commodity Exchange Act, 7 U.S.C. § 21(b)(10)). Initially, arbitration of customer disputes was limited to claims up to $5,000, but in 1978 the sum was increased to $15,000,[6] and in 1982, the limit on arbitrable customer's claims was deleted altogether,[7] with a view to enhancing the attractiveness of arbitration as a "viable forum for resolving customer claims." H.R. Rep. No. 565, 97th Cong., 2d Sess., part 1, at 56, *reprinted in* 1982 U.S.C.C.A.N. 3871, 3905.

To take another example, until the 1980s it was generally assumed that controversies over the validity or infringement of patents were not arbitrable, and several courts had so held. *See* P. Carmichael, *The Arbitration of Patent Disputes*, 38 Arb. J. 1, 3 nn. 3, 4, 5, 8 (March 1983) (citing cases). But when Congress considered the question in 1982, it expressly provided that parties to a dispute about the validity or infringement of a patent could agree in writing to settle such a dispute by arbitration in accordance with the Federal Arbitration Act. 35 U.S.C. § 294. The Report of the House Judiciary Committee accompanying the legislation stated:

> In the view of the Committee, a statutory authorization of voluntary agreements to arbitrate validity and infringement disputes would benefit both the parties to these disputes and the public.
>
> Statutory endorsement of arbitration agreements would assure the parties that they could avail themselves of the

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[6] Futures Trading Act of 1978, Pub. L. No. 95-505, § 22(2), 93 Stat. 865, 876.

[7] Futures Trading Act of 1982, Pub. L. No. 97-444, § 217(b), 96 Stat. 2294, 2307.

> numerous advantages of arbitration without the possibility of having to reargue the dispute in court. The advantages of arbitration are many: it is usually cheaper and faster than litigation; it can have simpler procedural and evidentiary rules; it normally minimizes hostility and is less disruptive of ongoing and future business dealings among the parties; it is often more flexible in regard to scheduling of times and places of hearings and discovery devices; and, arbitrators are frequently better versed than judges and juries in the area of trade customs and the technologies involved in these disputes.
>
> The enforcement of voluntary arbitration provisions would serve the public in two ways. First, the availability of arbitration with its numerous advantages will enhance the patent system and thus will encourage innovation. . . . Secondly, arbitration could relieve some of the burdens on the overworked Federal courts. . . .

H.R. Rep. No. 542, 97th Cong., 2d Sess. 13, *reprinted in* 1982 U.S.C.C.A.N. 765, 777.

In 1988, on recommendation of the Judicial Conference of the United States and the American Bar Association, Congress enacted 9 U.S.C. § 16, to allow immediate appeal from a District Court order denying a stay of litigation pending arbitration or denying a petition to compel arbitration, and to preclude appeal from an order granting a stay of litigation pending arbitration or directing arbitration to proceed. The purposes of this amendment included reinforcing the policy favoring arbitration by reducing the opportunity for a party to block or delay arbitration. *See* Mem. of Sen. Heflin, 134 Cong. Rec. S 16299 (daily ed. Oct. 14, 1988).

In short, Congress, like this Court, has seen the advantages of arbitration of commercial disputes pursuant to agreement, and has given no support to those who regard arbitration as "second class justice."

III.

The Arbitration System Provides a Fair, Effective and Expeditious Means of Resolving Disputes.

The experience of the last several decades demonstrates that arbitration is fair both to consumers and to other disputants. Based on its extensive experience in the administration of cases as well as its continuing surveys of user satisfaction, the AAA can confirm that arbitration provides due process and fair results to those who use it to resolve their disputes—whether large or small, rich or poor. The Appendix to this brief shows the geographic distribution of commercial disputes submitted to the Association in calendar year 1993, a breakdown of claims by dollar amounts, and a breakdown of the time elapsed from filing to award by the size of the claim. Of course the AAA's statistics do not include all controversies submitted to arbitration in the United States. But the sample is large enough to support the conclusion that arbitration of commercial disputes is practiced in all regions of the country, that it comprehends many small and medium-sized claims, and that in comparison with ordinary civil litigation in the United States (and particularly in comparison with jury trials), arbitration is substantially faster and therefore substantially less expensive.

A. Studies Have Demonstrated Widespread Satisfaction with Arbitration.

Studies conducted by the AAA and other organizations demonstrate widespread user satisfaction with the arbitration process. In 1985, a comprehensive survey was conducted jointly by the Dispute Avoidance and Resolution Subcommittee of the Forum Committee on the Construction Industry and the Construction Committee of the Litigation Section of the American Bar Association. Kenneth M. Cushman & Robert A. Rubin, *Report to the Membership of the Forum Committee on the Construction Industry*, Construction Lawyer, August 1987, at 9; *see also* Thomas J. Stipanowich, *Rethinking American Arbitration*, 63 Ind. L.J. 425 (1988). The resulting data represented the opinions of

some 600 attorney-members of these groups experienced in arbitration. For each of a number of categories related to speed, cost and quality, over two-thirds of those responding to the survey rated arbitration equal or superior to both jury trials and bench trials. Significantly, with regard to fairness of decision, 81.5% stated that arbitration was the same as or better than a jury trial, and 75.1% stated that arbitration was the same as or better than a bench trial. With regard to predictability of result, 77.8% rated arbitration as equal or superior to jury trials, and 69.9% rated arbitration as equal or superior to bench trials.

A portion of the survey focused on the reactions of the parties in interest, as well as their counsel, in construction cases in which the amount in dispute was less than $250,000. The survey asked the parties to rate their overall experience with arbitration in the areas of speed, economy, qualification of the arbitrators and fairness of the decision. In every one of those categories, over half of the parties responding to the survey rated their overall experience with the arbitration process as "excellent" or "good" (rather than "fair," "poor" or "very poor") in cases under $250,000. The parties' attorneys expressed similarly high levels of satisfaction with arbitration.[8]

A similar survey of attorney satisfaction with the arbitration process was conducted in 1988 by a joint task force of the Association of the Bar of the City of New York Arbitration and Alternative Dispute Resolution Committee, the New York County Lawyers' Association Arbitration and Alternative Dispute

[8] For construction disputes under $250,000, the following percentages of parties and attorneys rated their experience with the process as excellent or good in the various categories: time in which the case was first scheduled for hearing, parties 74.7%, attorneys 73.8%; speed of actual hearing, parties 67.7%, attorneys 77.1%; speed of arbitrators' decision, parties 71.7%, attorneys 74.6%; as an economic means of resolving disputes, parties 56.6%, attorneys 66.4%; qualification of arbitrators, parties 56.7%, attorneys 68.0%; fairness of decision, parties 52.7%, attorneys 51.7%. Attorneys but not parties were also asked about predictability of result; in this category, 42.8% rated arbitration as excellent or good.

Resolution Committee, and the AAA, focusing this time on participants in the larger, more complex commercial arbitrations. American Arbitration Ass'n, *Report and Recommendation of the Joint AAA Task Force on Procedures for Large, Complex Commercial Arbitrations* (1988). Attorneys were asked to rate their experience in arbitration, as compared with court trials, on a scale of one to five. With one exception (predictability of result in comparison with a federal bench trial), the average response rated arbitration above the midpoint of 3.0 in every category of performance (overall performance, time from start to finish, fairness of proceedings, predictability of result and overall cost including attorneys' fees) in comparison with every category of court trial (federal court bench trial, federal court jury trial, state court bench trial and federal court jury trial).

The Judicial Council of California has also conducted a study comparing arbitration to court resolution. The study, which looked at automobile insurance disputes, concluded that arbitration is faster, less expensive and about as fair and predictable as court adjudication, and has a high rate of acceptability among attorneys and insurance professionals. Judicial Council of California, *A Study of the Role of Arbitration in the Judicial Process* 74 (1972).

B. Arbitration Provides Consumers As Well As Business Firms a Fair, Speedy and Economical Forum To Resolve Their Disputes with Providers of Goods and Services.

The American Arbitration Association, as part of its organizational mission, administers thousands of arbitration cases of all types each year. Many of these cases are small, routine commercial matters, analogous to the dispute in the case at bar. As shown in the Appendix, of the 12,713 commercial cases that the Association administered in 1993, 8697, or 68%, involved claims of less than $50,000, and over half of those involved claims of less than $10,000. Most cases in which the claim was less than $50,000 were concluded in a single hearing, with an average time of 183 days (and a median time of 133 days) from the filing of the

claim to the issuance of the award. For cases in which the claim amount was less than $15,000, the average time from filing to award was 119 days, and the median time was 90 days.

The AAA regularly conducts consumer arbitrations in several areas, such as automobile "lemon laws." In these cases, too, the Association's experience demonstrates that arbitration can be a speedy, economical and fair way to make the consumer whole.

For example, the New York State Attorney General's Office oversees a "lemon law" arbitration program administered by the Association, and issues an annual report on the results. The data collected for 1993 indicate that the average disposition time (from filing to award) was 40 days for new-car cases and 54 days for used-car cases. Over the seven-year life of the new-car program and the four-year life of the used-car program, consumers prevailed in 56% of the new-car cases and 59% of the used-car cases. *See* N.Y. State Dep't of Law, *New York New Car Lemon Law Arbitration Program 1993 Annual Report*; N.Y. State Dep't of Law, *New York Used Car Lemon Law Arbitration Program 1993 Annual Report*. The State of Florida's "lemon law" arbitration program, which is not administered by the AAA, has shown similar success. *See* State of Fla. Office of Att'y Gen., *Lemon Law Arbitration Program Annual Report 1992*.

There is no reason to believe that a claim by a homeowner against a provider of extermination services, such as in the present case, would not be handled with equal fairness. Experience demonstrates that arbitration fulfills its promise of speed, economy and justice in regard to a broad range of commercial disputes. The support for the arbitral process that this Court and Congress have shown is well justified, and the fear of arbitration reflected in the decision of the Alabama Supreme Court in this and other cases has no factual support.

IV.

This Court Should Reject The Standard Adopted by the Alabama Supreme Court, Which Encourages "Litigation About Litigation" and Frustrates Congress's Intent.

As this Court has recognized, one of the chief reasons that parties choose arbitration is to avoid the delay and expense associated with litigation. *Southland Corp. v. Keating*, 465 U.S. at 7. The Arbitration Act was a congressional response to "agitation against the costliness and delays of litigation." H.R. Rep. No. 96, 68th Cong. 1st Sess. 1, 2 (1924). As the Senate report accompanying the legislation noted:

> The desire to avoid the delay and expense of litigation persists. . . . The settlement of disputes by arbitration appeals to big business and little business alike, to corporate interests as well as to individuals.

S. Rep. No. 536, 68th Cong. 1st Sess. 1, 3 (1924).

The Alabama Supreme Court's standard, which ties the application of the Act to the supposed factual issue of whether the parties "contemplated substantial interstate commerce" at the time they made the agreement to arbitrate, is particularly likely to cause extensive pre-arbitration litigation, in that it invites extensive judicial inquiry into the facts and circumstances surrounding an agreement to arbitrate and is substantially uncertain in its application to a wide range of cases. The volume of litigation on this question in Alabama demonstrates that such a standard is unsound and unworkable: in the past three years, the state's highest court has decided at least fourteen cases in which the "commerce" requirement of the Arbitration Act was a significant issue, including six cases in July and August of 1993 alone.[9]

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[9] In addition to the present case, decided August 13, 1993, these cases are *Ex parte Kent Corp.*, No. 1930240, 1994 Ala. LEXIS 97, 1994 WL 63458 (Ala. Mar. 4, 1994); *Ex parte Lorance*, 632 So. 2d 475 (Ala. Feb. 11, 1994); (continued...)

No matter how any particular case comes out, any standard that leads to fourteen cases in three years being taken to the state's highest court on the preliminary question of whether an agreement to arbitrate should be enforced frustrates the promise of arbitration and the intent of Congress to provide an expeditious and efficient means to resolve disputes. In the states that have adopted the "contemplated substantial interstate activity" standard, which was first suggested by Judge Lumbard in his concurring opinion in *Metro Industrial Painting Corp. v. Terminal Construction Co.*, 287 F.2d 382, 386 (2d Cir.), *cert. denied*, 368 U.S. 817 (1961), the result has been to create incentives to litigate about the applicability of the Federal Arbitration Act.[10] This has been true even in those states that permit specific enforcement of agreements to

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[9](...continued)
Henderson v. Superior Ins. Co., 628 So. 2d 365 (Ala. Aug. 20, 1993); *Lopez v. Home Buyers Warranty Corp.*, 628 So. 2d 361 (Ala. Aug. 20, 1993), *petition for cert. filed*, 62 U.S.L.W. 3430 (U.S. Dec. 22, 1993) (No. 93-995); *Terminix Int'l Co. Ltd. Partnership v. Jackson*, 628 So. 2d 357 (Ala. Aug. 13, 1993), *petition for cert. filed*, 62 U.S.L.W. 3430 (U.S. Dec. 22, 1993) (No. 93-1000); *Ex parte Jones*, 628 So. 2d 316 (Ala. July 16, 1993); *Continental Grain Co. v. Beasley*, 628 So. 2d 319 (Ala. July 16, 1993); *First Real Estate Corp. v. Brown Marx Tower Ltd. Partnership*, 620 So. 2d 648 (Ala. May 7, 1993); *Garikes, Wilson & Atkinson, Inc. v. Episcopal Found. of Jefferson County, Inc.*, 614 So. 2d 447 (Ala. Mar. 5, 1993); *A.J. Taft Coal Co. v. Randolph*, 602 So. 2d 395 (Ala. July 31, 1992); *Ex parte Brice Building Co.*, 607 So. 2d 132 (Ala. July 17, 1992); *Maxus, Inc. v. Sciacca*, 598 So. 2d 1376 (Ala. May 15, 1992); *Ex parte Clements*, 587 So. 2d 317 (Ala. Aug. 30, 1991).

[10] *See, e.g., ESAB Automation, Inc. v. Hesco Sales, Inc.*, 582 So. 2d 810, 810 (Fla. App. 1991); *United Servs. Gen. Life Co. v. Bauer*, 568 So. 2d 1321, 1322-23 (Fla. App. 1990); *Acton CATV, Inc. v. Wildwood Partners, Ltd.*, 508 So. 2d 1274, 1275-76 (Fla. App.), *review denied*, 518 So. 2d 1273 (Fla. 1987); *Riverfront Properties Ltd. v. Max Factor III*, 460 So. 2d 948, 952-54 (Fla. App. 1984); *R.J. Palmer Constr. Co. v. Wichita Band Instrument Co.*, 642 P.2d 127, 130-31 (Kan. App. 1982); *Loche v. Dean Witter Reynolds, Inc.*, 526 N.E.2d 1296, 1299-1300 (Mass. App. Ct. 1988); *Burke County Public Schools Bd. of Educ. v. Shaver Partnership*, 279 S.E.2d 816, 822 (N.C. 1981); *Paramore v. Inter-Regional Fin. Group Leasing Co.*, 316 S.E.2d 90, 92 (N.C. App. 1984); *Cohoon v. Ziman*, 298 S.E.2d 729, 730-31 (N.C. App.), *review denied*, 301 S.E.2d 388 (N.C. 1983).

arbitrate, because of exceptions or procedural or jurisdictional quirks in the state arbitration statutes.[11]

Though the Alabama Supreme Court's standard is particularly damaging, any standard that generates significant uncertainty about the scope of the Arbitration Act has the potential to defeat the advantages of speed and economy that prompt parties to choose arbitration. Only by recognizing that the Arbitration Act extends to the limits of Congress's Commerce Clause powers can this Court give full effect to

> Congress' clear intent, in the Arbitration Act, to move the parties to an arbitrable dispute out of court and into arbitration as quickly and easily as possible.

Moses H. Cone, 460 U.S. at 22.

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[11] *See, e.g., Action CATV*, 508 So. 2d at 1275-76 (refusing to order arbitration under Federal Arbitration Act because parties did not contemplate substantial interstate activity, and under Florida arbitration statute, because contract called for arbitration in another state); *Riverfront Properties*, 460 So. 2d at 952-54 (refusing to apply Federal Arbitration Act for same reason; Florida law did not permit enforcement of agreement to arbitrate because contract contained choice-of-law clause specifying another state's law); *Paramore*, 316 S.E.2d at 92 (refusing to apply Federal Arbitration Act for same reason; North Carolina law required pre-arbitration judicial decision on defenses of fraud, undue influence and unconscionability).

CONCLUSION

For the reasons stated, this Court should make clear that in all commercial transactions within the reach of Congress's commerce powers, an agreement to arbitrate will be enforced in accordance with the Arbitration Act.

Accordingly, the Association respectfully urges the Court to reverse the judgment of the Supreme Court of Alabama and remand the case for further proceedings consistent with the principles discussed herein.

Respectfully submitted,

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May 19, 1994

APPENDIX

AAA COMMERCIAL CASE REPORT

January 1993 to December 1993

Geographical Distribution

AAA Office	Number of Cases Filed	Total Amount of Claims and Counterclaims
Atlanta	231	$ 68,596,374.42
Boston	408	773,569,038.51
Charlotte	166	43,461,731.92
Chicago	469	108,549,139.18
Cincinnati	221	52,621,715.03
Cleveland	168	107,173,186.30
Dallas	336	170,807,393.07
Denver	224	595,428,251.56
Detroit	399	92,795,730.54
Garden City	172	30,502,055.30
Hartford	232	32,746,664.24
Hawaii	184	299,132,315.15
Houston	152	144,738,466.54
Kansas City	100	24,179,518.94
Las Vegas	56	13,690,374.61
Los Angeles	1,631	621,765,580.34
Miami	537	102,786,765.46
Minneapolis	666	20,008,504.57
Nashville	75	14,458,804.31
New Jersey	394	80,906,176.78
New Orleans	113	78,364,709.49
New York	1,105	1,052,054,582.21
Orange County	385	55,416,993.99
Orlando	191	49,396,276.98

Philadelphia	380	71,984,959.42
Phoenix	203	22,885,158.53
Pittsburgh	212	121,319,103.28
Providence	34	4,483,858.42
Salt Lake	94	9,451,416.13
San Diego	405	73,848,690.65
San Francisco	1,505	780,430,100.79
Seattle	367	50,537,746.40
St. Louis	86	37,040,834.14
Syracuse	187	19,235,043.30
Washington, D.C.	504	234,109,184.79
White Plains	121	19,252,946.22
TOTAL	12,713	$ 6,077,729,391.51

Breakdown of Amounts of Claims

Amount of Claims	Number of Cases Filed	Percent of Cases Filed
$1 - $10,000	4,442	35%
$10,001 - $50,000	4,255	33%
$50,001 - $100,000	1,022	8%
$100,001 - $500,000	1,737	14%
$500,001 - $1,000,000	260	2%
$1,000,000 and over	372	3%
No Amount Disclosed	625	5%

1993 PROCESSING TIME (IN DAYS) FROM FILING TO AWARD IN AAA COMMERCIAL CASES

Claim Amount	No. of Cases	Avg. No. of Days	Median No. of Days	Avg. No. of Hrgs.
$1 - $15,000	1654	119	90	1
$15,001 - $50,000	1012	183	133	1
$50,001 - $100,000	283	293	232	1
$100,001 - $500,000	451	312	245	2
$500,001 - $1,000,000	86	496	384	3
Over $1,000,000	113	475	328	4
Undetermined	727	249	169	1
OVERALL	4,326	204	133	1

(8)

Supreme Court, U.S.
FILED
MAY 18 1994
OFFICE OF THE CLERK

No. 93-1001

In The

Supreme Court of the United States

October Term, 1993

ALLIED-BRUCE TERMINIX COMPANIES, INC., ET AL.,

Petitioners,

v.

G. MICHAEL DOBSON, ET AL.,

Respondents.

On Writ Of Certiorari
To The Supreme Court Of Alabama

BRIEF OF THE ALABAMA WATER AND WASTEWATER INSTITUTE, THE ALABAMA MANUFACTURED HOUSING INSTITUTE AND THE ALABAMA PEST CONTROL ASSOCIATION AS *AMICI CURIAE* IN SUPPORT OF PETITIONERS

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QUESTION PRESENTED

Section 2 of the Federal Arbitration Act, 9 U.S.C. § 2, makes an agreement to arbitrate enforceable, as a matter of federal law, provided that it is part of "a contract evidencing a transaction involving commerce." The question presented here is as follows:

Whether the Alabama Supreme Court correctly held - contrary to the view taken by the majority of state and federal courts - that Section 2 is inapplicable to contracts otherwise involving interstate commerce if the parties did not "contemplate[] substantial interstate activity" at the time they entered the contract.

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No. 93-1001

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G. MICHAEL DOBSON, ET AL.,

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On Writ Of Certiorari
To The Supreme Court Of Alabama

BRIEF OF THE ALABAMA WATER AND WASTEWATER INSTITUTE, THE ALABAMA MANUFACTURED HOUSING INSTITUTE AND THE ALABAMA PEST CONTROL ASSOCIATION AS *AMICI CURIAE* IN SUPPORT OF PETITIONERS

INTEREST OF AMICI CURIAE

The Alabama Water and Wastewater Institute (hereinafter "AWWI"), formerly known as the Alabama Water and Sewer Institute, is a non-profit organization representing thirteen of the largest water producers in the State of Alabama. Its members are public corporations and municipal boards organized and existing pursuant to Acts of the Legislature of Alabama for the purpose of operating water and/or sanitary sewer facilities within the State of Alabama. AWWI has an interest in this case in

that its members regularly enter into contracts in the State of Alabama. Said contracts include agreements for engineering services and other professional services, for construction of public facilities, and for the purchase and lease of real and personal property. The members of AWWI have an interest in state court enforcement of agreements to submit disputes arising from these contracts to binding arbitration in order to control the increasing costs of litigation that drain funds designated for public purposes.

The Alabama Manufactured Housing Institute (hereinafter "AMHI") is a non-profit trade association representing all segments of the manufactured housing industry. Its members include nearly 450 manufactured home manufacturers, retailers, parts suppliers, providers of services including delivery and installation, finance and insurance companies, park owners and developers. AMHI has an interest in this case in that the members of AMHI regularly enter into contracts in the State of Alabama. The members of AMHI have an interest in state court enforcement of agreements to submit disputes arising from these contracts to binding arbitration in order to control the increasing costs of litigation affecting all aspects of the manufactured home industry.

The Alabama Pest Control Association (hereinafter "APCA") is a non-profit trade association representing over eighty-five percent of the licensed pest control operators in the State of Alabama, including large, international companies as well as local sole proprietorships. Pest control companies of all sizes are represented on APCA's five member executive board. APCA was formed in 1947 for the purpose of uniting the growing pest

control industry in a concern for the safety and health of customers and pest control operators. Since its formation, APCA has been an instrumental force in advancements in training, equipment and chemical development fundamental to this goal.

APCA has an interest in this case in that its members regularly enter into termite bonds with customers in the State of Alabama that contain predispute arbitration clauses substantially similar to that at issue in the instant case. These termite bonds are typically issued to customers at the time of initial treatment of their homes for termites and may be terminated by the pest control company only for cause. Once a customer purchases a termite bond, he may renew it annually, in most cases indefinitely, without fear of cancellation, so long as he maintains his home. In addition, many of these bonds are assignable by a homeowner to subsequent purchasers.

The members of APCA have an interest in the courts of Alabama enforcing agreements to submit disputes arising from these termite bonds to binding arbitration in order to control the increasing costs of litigation affecting all aspects of the pest control industry. The Alabama Supreme Court's refusal to recognize the application of the Federal Arbitration Act to these bonds, many of which have been in force for several years, substantially impairs the rights of the members of APCA under said contracts as well as the rights of consumers of pest control services to affordable prices. APCA estimates that the cost to Alabamians in 1992 for control of household and structural pests and in damages caused by structural pests exceeded four hundred sixty million dollars ($460,000,000.00).

Petitions for Writs of Certiorari to the Alabama Supreme Court involving the same issue presented in this case are pending before this Court in *Terminix International Company Limited Partnership and Allied-Bruce Terminix Companies, Inc., v. Jackson*, 628 So.2d 357 (Ala. 1993), and in *Lopez v. Home Buyers Warranty Corporation*, 628 So.2d 361 (Ala. 1993). The arguments presented by AWWI, AMHI, and APCA also support the positions advocated by the said petitioners in these related cases.

If the arguments of AWWI, AMHI, and APCA are approved by this Court, the decision of the Alabama Supreme Court must be reversed.

SUMMARY OF THE ARGUMENT

This Court has held that the Federal Arbitration Act applies to the full extent of the power of Congress over interstate commerce. *Perry v. Thomas*, 482 U.S. 483, 490 (1987); *Southland Corp. v. Keating*, 465 U.S. 1, 13 (1984); *Prima Paint Corp. v. Flood & Conklin Manufacturing Co.*, 388 U.S. 395, 401 (1967). The holding of the Supreme Court of Alabama in the case of *Allied-Bruce Terminix Companies, Inc., v. Dobson*, 628 So.2d 354 (Ala. 1993), undermines the broad and liberal federal policy favoring the enforceability of arbitration agreements by limiting the application of the Federal Arbitration Act to transactions where the parties actually contemplated, at the time they entered into the contract, substantial interstate activity. The Supreme Court of Alabama's restriction on the

application of the Federal Arbitration Act is clearly contrary to the precedent of this Court.

ARGUMENT

The Federal Arbitration Act (hereinafter "FAA") provides that arbitration clauses in contracts "involving commerce," where commerce is defined as "commerce among the several States," shall be enforceable. 9 U.S.C. § 2. The issue in the present case has arisen because the Alabama Supreme Court has interpreted the phrase "contracts involving commerce among the several States," as used in the FAA, to invoke less power than Congress has under the Commerce Clause to regulate activities "affecting" interstate commerce. In short, the Alabama Supreme Court has disregarded the precedent of this Court requiring that the FAA be applied to the full extent of Congressional power under the Commerce Clause.

This Court stated in *Perry v. Thomas*, 482 U.S. 483, 490 (1987), that the FAA provides "for the enforcement of arbitration agreements within the full reach of the Commerce Clause." It is clear that the FAA is based upon the commerce power of Congress, and that contracts are to be construed liberally in favor of arbitration. *Southland Corp. v. Keating*, 465 U.S. 1, 12-13 (1984) ("[T]he [FAA] was an exercise of the Commerce Clause power."); *Moses H. Cone Memorial Hospital v. Mercury Construction Co.*, 460 U.S. 1, 24 (1983) ("Section 2 [of the FAA] is a congressional declaration of a liberal federal policy favoring arbitration agreements, notwithstanding any state substantive or procedural policies to the contrary."); *Prima Paint Corp. v.*

Flood & Conklin Mfg. Co., 388 U.S. 395, 401 (1967) ("It is clear beyond dispute that the federal arbitration statute is based upon and confined to the incontestable federal foundations of 'control over interstate commerce and over admiralty.' "); *See also Bernhardt v. Polygraphic Company*, 350 U.S. 198, 200-201 (1956). Moreover, this Court has stated that "[t]he purpose of the [FAA] was to assure those who desired arbitration and whose contracts related to interstate commerce that their expectations would not be undermined by . . . state courts." *Southland Corp. v. Keating*, 465 U.S. 1, 13 (1984).

A majority of the federal circuit courts of appeals and federal district courts have interpreted the term "involving commerce" to bring within the FAA all contracts that Congress could constitutionally regulate under the Commerce Clause.[1] AWWI, AMHI, and APCA urge this Court

[1] *E.g., Del E. Webb Const. v. Richardson*, 823 F.2d 145, 147 (5th Cir. 1987) (A contract comes under the FAA so long as it simply relates to interstate commerce.); *Mesa Operating Ltd. Partnership v. Louisiana Intrastate Gas Corp.*, 797 F.2d 238, 243 (5th Cir. 1986) ("Commerce" under the FAA includes all contracts relating to interstate commerce.); *American Airlines, Inc. v. Louisville and Jefferson County Air Board*, 269 F.2d 811 (6th Cir. 1959) (FAA was enacted in exercise of Congress' plenary power over interstate commerce.); *Snyder v. Smith*, 736 F.2d 409 (7th. Cir. 1984) (The breadth of "involving commerce" is equated with the extent of Congress's power to regulate under the commerce clause; Congress intended the FAA to extend to all contracts that it could constitutionally regulate.); *First Investors Corp. v. American Capital Financial Services, Inc.*, 823 F.2d 307 (9th Cir. 1987) (FAA governs agreements "affecting" interstate commerce.); *Foster v. Turley*, 808 F.2d 38 (10th Cir. 1986) (Requirement of FAA that underlying transaction involve commerce is to be broadly construed so as to be coextensive with congressional power to regulate under the Commerce Clause.); *Shatel Corp. v. Mao Ta Lumber and Yacht Corp.*, 697 F.2d 1352, 1354 (11th Cir. 1983) ("Commerce" includes any intrastate transaction which "affects" interstate commerce.); *G.D. Searle & Co. v. Metric Constructors, Inc.*, 572 F.Supp. 836 (N.D.Ga. 1983) (It has consistently been noted that federal policy favors arbitration and that the statute should be broadly applied.); *Fairchild & Co., Inc. v. Richmond, F. & P.R. Co.*, 516 F.Supp. 1305 (D.C.D.C. 1981) ("[I]nvolving commerce" as used in FAA is not to be narrowly construed as "commerce" reaches not only the actual physical interstate shipment of goods but also contracts relating to interstate commerce.); *John W. Johnson, Inc. v. 2500 Wisconsin Ave.*, 231 F.2d 761 (D.C.Cir. 1956).

to sustain the validity of the majority position as consistent with Congressional intent as expressed in the FAA.

Where courts have taken a more restrictive position than that of the majority and have interpreted the FAA to have less force than the Commerce Clause permits, the outcome has been an arbitrary and uncertain counting of the contacts between the contract and the states other than the one in which it is being, or was intended to be, performed in order for the trial court to determine whether the FAA preempts state law and allows arbitration to proceed.[2] Although such a fact finding process

[2] *E.g., Dickstein v. DuPont*, 443 F.2d 783 (1st Cir. 1971) (Contract was not a transaction involving commerce since there was no movement of goods across state lines.); *Thomas O'Connor & Co., Inc. v. Insurance Co. of North America*, 697 F.Supp. 563 (D.Mass. 1988) (Construction contract involved commerce where New York contractor performed work in New Jersey, materials came from outside New Jersey, and subcontractor was citizen of Massachusetts.); *New Castle County v. U.S. Fire Ins. Co.*, 728 F.Supp. 318 (D.Del. 1989) (Settlement agreement between insurer and county, who were citizens of different states, which involved at least $184,000 was a contract involving commerce

may be less subjective than the "contemplation of the parties" test adopted by the Alabama Supreme Court, the

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under the FAA.); *Goodwin v. Elkins & Co.*, 730 F.2d 99, *cert. denied* 105 S.Ct. 118 (3rd Cir. 1984); *compare Kirschner v. West Co.*, 185 F.Supp. 317, 319 (D.C.Pa. 1960) ("Commerce" means the type of commerce which is within federal jurisdiction, that is, interstate or foreign commerce.); *AM. Home Assur. v. Vecco Concrete Const., Etc.*, 629 F.2d 961 (4th Cir. 1980) (Transaction between Delaware Corporation, with its principal place of business in Alabama, and Virginia Corporation, which included subcontracts and purchase orders for products and equipment shipped to Virginia from Maryland, Alabama, Utah, Missouri and California, which employed non-residents in the project, and used a New York bonding company to guarantee performance, clearly demonstrated that the contract was one evidencing a transaction involving interstate commerce as contemplated by the FAA.); *Mutual Reinsurance Bureau v. Great Plains Mut. Ins. Co., Inc.*, 750 F.Supp. 455 (D.C.Kansas 1990) (Reinsurance agreement between two insurers involved interstate commerce within the FAA even though contract negotiations transpired within Kansas, where parties were of diverse citizenship, the agreement was originally drafted in Illinois, and business was transacted over the telephone and through the mail.); *Axtell v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 744 F.Supp. 194, 195 (E.D.Ark. 1989) (Customer agreement signed by investors that contained arbitration agreement affected "commerce" within the meaning of the FAA.); *compare Seymour v. Gloria Jean's Coffee Bean Franchising Corp.*, 732 F.Supp. 988 (D.Minn. 1990) (Federal Arbitration Act is based on congressional power to regulate interstate commerce.); *England v. Dean Witter Reynolds, Inc.*, 811 S.W.2d 313 (Ark. 1991) (Employment contract to work for securities broker was contract involving interstate commerce.); *McEntire v. Monarch Feed Mills*, 631 S.W.2d 307 (Ark. 1982) (Contract involved interstate commerce where Missouri based grain purchaser with manufacturing facilities in Missouri and Arkansas contracted to purchase grain from farmer in Arkansas for delivery to its manufacturing plant in Arkansas.); *Ayers v. Prudential-Bache Securities*, 762 P.2d 743 (Colo.App. 1988) (citing *Robinson v. Bache*

practical result may well be lengthy trial court involvement in a fact finding expedition that ultimately thwarts the goals of the FAA.

& Co., 227 F.Supp. 456 (S.D.N.Y. 1964) (A contract between a brokerage firm and its customer is a contract evidencing a transaction involving commerce within the meaning of the FAA.); *Helca Min. Co. v. Bunker Hill Co.*, 617 P.2d 861 (Idaho 1980) (FAA applied to contract between two mining companies because contract clearly involved interstate commerce.); *Kodak Min. Co. v. Carrs Fork Corp.*, 669 S.W.2d 917 (Ky. 1984) (A contract was found to involve interstate commerce where the parties were incorporated in different states, arbitrators under the agreement were selected by federal judges from different states, and the leases in question involved interstate commerce.); *Kaufman v. The Chicago Corp.*, 466 N.W.2d 726 (Mich. App. 1991) (Employment contract with member of national stock exchange involves interstate commerce.); *Scanlon v. P&J Enterprises, Inc.*, 451 N.W.2d 616 (Mich.App. 1990) (Transfer of market expertise from Tennessee to Michigan through a franchise agreement was a transaction in interstate commerce.); *Thayer v. American Financial Advisers, Inc.*, 322 N.W.2d 599, 603-604 (Minn. 1982); *Downey v. Christensen*, 825 P.2d 557 (Mont. 1992) (Dealership agreement was contract evidencing interstate commerce.); *compare William Gibson Jr. Inc. v. James Graff Com.*, 780 P.2d 1131 (Mont. 1989) (Where 5% of business was conducted out of state there was sufficient activity to affect interstate commerce under the FAA.); *Dowd v. First Omaha Securities Corp.*, 495 N.W.2d 36 (Neb. 1993) (Written contract to buy and sell securities is contract directly involved in interstate commerce.); *Dean Witter Reynolds, Inc. v. Roven*, 609 P.2d 720 (N.M. 1980) (Contract concerning commodity trading of gold futures is contract involving commerce under the FAA.); *Trombetta v. Conkling*, 586 N.Y.S.2d 461 (Supp. 1992) (Disputes arising out of employment in the securities market involve interstate commerce.); *Episcopal Housing Corporation v. Federal Insurance Company*, 239 S.E.2d 647 (S.C. 1977) (A construction contract evidences transactions in commerce where labor, supplies and materials from all over the country were

The financial risks of the party seeking to enforce a predispute arbitration clause may force the party to forego the battle over enforceability of the clause for fear that it may have doubled its litigation costs if the trial court ultimately denies the motion to arbitrate. As noted by this Court in *Moses H. Cone Memorial Hospital v. Mercury Construction Corp.*, 460 U.S. 1, 22 (1983), the FAA is designed to allow "parties to an arbitrable dispute [to move] out of court and into arbitration as quickly and easily as possible." In *Southland Corp. v. Keating*, 465 U.S. 1, 7 (1984), this Court observed that " . . . allowing one party to ignore [an arbitration clause in] the contract and resort to the courts . . . could lead to prolonged litigation, one of the very risks the parties, by contracting for arbitration, sought to eliminate."

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utilized in the construction.); *Tennessee River Pulp & Paper v. Eichleay*, 637 S.W.2d 853 (Tenn. 1982) (Contract in this case found to evidence a transaction involving interstate commerce where contract exceeded $15,000,000.00 and was between two Delaware corporations; the plaintiff's home office was in Illinois; defendant's home office was in Pennsylvania; the materials used, the labor employed, and the subcontractors involved, in substantial part, came from outside Tennessee; substantial quantities of materials and supplies came from 26 different states; 34% of all materials and supplies were purchased outside of Tennessee.); *International Bank of Commerce v. Caquias*, 846 S.W.2d 496 (Tex.App.-Corpus Christi 1993) (Where loan funds provided under note were derived from interstate financial markets the loan was a transaction involving commerce.); *See also Jack B. Anglin Co., Inc. v. Tipps*, 842 S.W.2d 266 (Tex. 1992); *Kinsey v. Bradley*, 765 P.2d 1329 (Wash.App. 1989) (Commodities account customer agreement involved interstate commerce.); *See also Wineland v. Marketex International, Inc.*, 627 P.2d 967 (Wash.App. 1981); *See also Allison v. Medicab International, Inc.*, 597 P.2d 380 (Wash. 1979).

The restrictive standard for applying the FAA adopted by the Alabama Supreme Court goes even farther, requiring the trial judge to engage in an analysis of the subjective intent of the parties. If this standard is sustained, Alabama courts may determine that the issue of the parties' intent is itself a jury question. The subjective nature of this test is exaggerated by the inclusion of the "*substantial* interstate activity" requirement. Even those litigants who were aware of the potential involvement of interstate commerce in the performance of the contract when it was entered may easily defeat motions to enforce arbitration clauses by denying that they contemplated "*substantial* interstate activity," since "substantial" is itself a subjective word open to the litigant's own interpretation.

The adoption of this standard represents a revival of the Alabama Supreme Court's longstanding hostility towards arbitration. In *Ex parte Alabama Oxygen*, 433 So.2d 1158 (Ala. 1983), *vacated and remanded*, 465 U.S. 1016 (1984), this Court was called upon to reverse the Alabama Supreme Court's opinion that the FAA did not preempt state law prohibiting enforcement of arbitration agreements. In the ten year period since, the Alabama Supreme Court has gradually returned to its original stance on the issue. Under Alabama law, the specific enforcement of a predispute arbitration agreement violates public policy. See *Alabama Code* (1975), section 8-1-41(3); *Old Republic Insurance Company v. Lanier, et al.*, [Ms. 1921387, April 29, 1994], ___ So.2d ___ (Ala. 1994). Even when the application of the FAA is undisputed, the Alabama court continues to look to the "strong public policy against the use

of predispute arbitration agreements" to restrict the coverage of arbitration provisions. *Old Republic Insurance Company*, Slip Op. at 9.

The Alabama Supreme Court's recent opinion in *Old Republic Insurance Company* illustrates the court's mission to provide every route possible to litigants to avoid FAA pre-emption of this "strong public policy." The error in the court's reasoning was first recognized by Justice Maddox in 1984 in his dissenting opinion in *Ex parte Alabama Oxygen Co.*, 433 So.2d 1158 (Ala. 1983) (Maddox, J., dissenting), *vacated and remanded*, 465 U.S. 1016 (1984), which opinion was adopted by the majority on remand from this Court. *Ex parte Alabama Oxygen Co.*, 452 So.2d 860 (Ala. 1984).

Justice Maddox has again recognized the error of the majority in his dissenting opinion in *Old Republic Insurance Company*, Slip Op. at 14-19, by noting that,

> [i]n *Moses H. Cone Mem. Hospital v. Mercury Constr. Corp.*, 460 U.S. 1, 24, 103 S. Ct. 927, 941, 74 L. Ed. 2d 765, 785 (1983), the Supreme Court of the United States stated that § 2 of the FAA stands for "a liberal federal policy favoring arbitration agreements, notwithstanding any state substantive or procedural policies to the contrary" and "creates a body of federal substantive law of arbitrability, applicable to any arbitration agreement within the coverage of the Act." Therefore, I am of the opinion that if the contract involved is one involving interstate commerce and the contract contains an arbitration agreement voluntarily entered into by the parties, federal policy favoring arbitration agreements must be applied, notwithstanding what the majority

> refers to as "our strong public policy against the use of pre-dispute arbitration agreements."

The erroneous subjective standard adopted by the Alabama Supreme Court originated in the Second Circuit Court of Appeal's opinion in *Metro Indust. Painting v. Terminal Const. Co., Inc.*, 287 F.2d 382 (2nd Cir. 1961), *cert. denied*, 368 U.S. 817 (1961), and has not been adopted by any federal circuit court of appeals. In *Metro*, Chief Judge Lumbard, in his concurring opinion, created the restrictive standard stating that a contract involves interstate activity if at the time the parties entered into it and accepted the arbitration clause, they contemplated substantial interstate activity. The majority did not address the issue, stating that irrespective of whether Congress intended the coverage of the FAA to be as broad as the constitutional dimensions of the commerce power, the facts found by the judge below were sufficient to support a finding that the transaction evidenced by the contract was within the statutory requirements of the FAA.

With litigation expenses rising and increasing the costs of services and products offered by AWWI, AMHI, and APCA members to consumers of their products and services, arbitration is an increasingly popular alternative for dispute resolution. In order for arbitration to be effective, however, the cost of enforcing arbitration agreements at the trial court level must not itself be excessive. The test adopted by the Alabama Supreme Court requires a mini-trial of ancillary issues that may prove as expensive as a trial on the merits in many cases.

The proper standard for courts to apply in determining whether a contract comes within the provisions of the

FAA is whether that contract relates to or affects interstate commerce in any way. Any interstate activity or connection with interstate activity such as a party being from another state, purchase and transportation of materials from another state, or the production of goods within one state for ultimate consumption in another state is sufficient to invoke the coverage of the FAA. The mere fact that the work under a contract is to be performed solely within one state should not prevent the application of the FAA to that contract if the activity under the contract, either through the involvement of parties from other states or through the use of goods from other states, affects or relates to interstate commerce. *Perry v. Thomas*, 482 U.S. 483, 490 (1987); *Southland Corp. v. Keating*, 465 U.S. 1, 13 (1984); *Prima Paint Corp. v. Flood & Conklin Manufacturing Co.*, 388 U.S. 395, 401 (1967); *Mesa Operating Ltd. Partnership v. Louisiana Intrastate Gas Corp.*, 797 F.2d 238, 243 (5th Cir. 1986); *Snyder v. Smith*, 736 F.2d 409, 417-420 (7th Cir. 1984).

CONCLUSION

For the reasons set forth above, this Court should reverse the decision of the Supreme Court of Alabama.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1993

ALLIED-BRUCE TERMINIX COMPANIES, INC., AND TERMINIX INTERNATIONAL COMPANY,

Petitioners,

v.

G. MICHAEL DOBSON, WANDA C. DOBSON, STEVEN GWIN AND JAN GWIN,

Respondents.

On Writ of Certiorari To The Supreme Court of Alabama

BRIEF *AMICI CURIAE* OF THE AMERICAN BANKERS ASSOCIATION, THE AMERICAN FINANCIAL SERVICES ASSOCIATION, AND ITT CONSUMER FINANCIAL CORPORATION IN SUPPORT OF PETITIONERS

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INTEREST OF *AMICI CURIAE**

The American Bankers Association ("ABA") is the principal national trade association of the commercial banking industry in the United States. It has members located in each of the fifty states and the District of Columbia and includes banks of all types and sizes—money centers, regional and community banks. ABA members hold approximately ninety-five percent of the domestic assets of United States banks. The ABA frequently appears in litigation as either a party or as *amicus curiae* where the issues raised are of widespread importance and concern to banks or consumers of banking services. ABA members regularly include arbitration agreements in their loan and other contracts.

The American Financial Services Association ("AFSA") was organized in 1916, and represents more than 300 companies operating more than 10,000 offices engaged in the extension of consumer credit throughout the United States. These companies range from independently-owned consumer finance offices to the nation's largest financial services, retail, and automobile companies. The AFSA's membership includes national and state banks that operate multistate consumer credit programs. AFSA's members frequently rely on arbitration agreements as dispute resolution mechanisms.

ITT Consumer Financial Corporation ("ITT") is a nationwide business, with headquarters in Minnesota, that provides consumer loans and related services. A substantial number of ITT's consumer loan contracts

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* Counsel to the parties have consented to the filing of this brief. Letters of consent have been filed with the Clerk.

contain arbitration agreements. The efficiency of dispute resolution available from arbitration is essential to ITT's ability to offer consumer loans on competitive terms. ITT has been involved in litigation challenging the validity of its arbitration agreements under various state-law barriers to arbitration. ITT has argued that such state laws and policies are preempted by the broad reach of the Federal Arbitration Act. *See, e.g.*, *Patterson* v. *ITT Consumer Fin. Corp.*, 14 Cal. App. 4th 1659, 18 Cal. Rptr. 2d 563 (1993), *cert. denied*, 114 S. Ct. 1217 (1994).

Amici curiae have a strong interest in the enforcement of arbitration agreements in all of their contracts. They file this brief because the policy adopted by the Alabama Supreme Court in this case materially narrows the scope and effectiveness of the Federal Arbitration Act. Failure to overturn that policy inevitably would subject substantial numbers of contracts that involve interstate commerce to state statutes and common law hostile to the enforcement of arbitration agreements.

SUMMARY OF ARGUMENT

The Federal Arbitration Act ("FAA" or the "Act"), 9 U.S.C. §§ 1, *et seq.*, applies to arbitration provisions in "contract[s] evidencing transaction[s] involving commerce." *Id.* § 2. The Alabama Supreme Court has adopted a rule that the Act applies only when the parties to a contract "*contemplated substantial* interstate activity." Pet. App. 4a (emphasis added). The "contemplation-of-the-parties" test is an anachronism that cannot be reconciled with the FAA and the strong federal policy favoring the enforcement of arbitration agreements.

The contemplation-of-the-parties test was first promulgated to restrict the scope of the FAA at a time when some courts were uncertain about the preemptive effect of the Act. However, in the 30 years since Judge Lumbard proposed the test in his concurring opinion in *Metro Industrial Painting Corp.* v. *Terminal Construction Co.*, 287 F.2d 382 (2d Cir.), *cert. denied*, 368 U.S. 817 (1961), this Court has removed any doubt about the broad effect of the FAA. The Court has established decisively that the FAA "is a congressional declaration of a liberal federal policy favoring arbitration agreements, notwithstanding any state substantive or procedural policies to the contrary." *Moses H. Cone Memorial Hosp.* v. *Mercury Constr. Corp.*, 460 U.S. 1, 24 (1983). In contrast, the Alabama Supreme Court has acknowledged that it adopted the contemplation-of-the-parties test precisely because of Alabama's strong public policy *against* arbitration.

The FAA was enacted nearly 70 years ago to end the hostility toward arbitration that Alabama and certain other states continue to display today. The Act and the strong federal policy that it enunciates demand that the statute be applied coextensively with Congress' Commerce Clause powers. The cost of applying the FAA more narrowly, as the Alabama Supreme Court has done in this case, is to allow the application of a variety of hostile state laws to prevent the enforcement of arbitration agreements within the scope of the federal interest. Alabama's narrow, subjective and elusive test both undermines federal policy and makes the Act's application uncertain and inconsistent.

Where parties to a contract involving interstate commerce agree to arbitrate differences between them, the policy of the FAA is frustrated if the arbitration provision is not enforced, regardless of the claims by either of the parties concerning their "contemplation" of interstate commerce. Alabama's policy *against* arbitration must not be allowed to trump federal policy in *favor* of arbitration.

ARGUMENT

I

THE CONTEMPLATION-OF-THE-PARTIES TEST IS A REMNANT OF AN ANACHRONISTIC AND NARROW VIEW OF THE FEDERAL ARBITRATION ACT THAT CONTRADICTS THE BROAD FEDERAL POLICY FAVORING ARBITRATION

Early in this century, the increasing complexity of the American economy and the growing expense and delay of litigation created great pressures in favor of more efficient mechanisms for the resolution of disputes. Arbitration offered an important alternative for dispute resolution, but its full effectiveness was stymied by the refusal of common-law courts to enforce arbitration agreements. Therefore, Congress passed the FAA in 1925 "to reverse the longstanding judicial hostility to arbitration agreements that had existed at English common law and had been adopted by American courts, and to place arbitration agreements upon the same footing as other contracts." *Gilmer* v. *Interstate/Johnson Lane Corp.*, 500 U.S. 20, 24 (1991). *See also Dean Witter Reynolds Inc.* v. *Byrd*, 470 U.S. 213, 219-220 & n.6 (1985).

The FAA expressed congressional recognition not only of the great value of arbitration to the efficient

flow of commerce but also of the costs imposed by judicial hostility toward arbitration. *See* S. Rep. No. 536, 68th Cong., 1st Sess. 3 (1924) ("The settlement of disputes by arbitration appeals to big business and little business alike, to corporate interests as well as to individuals."); H.R. Rep. No. 96, 68th Cong., 1st Sess. 2 (1924) ("It is practically appropriate that the action should be taken at this time when there is so much agitation against the costliness and delays of litigation. These matters can be largely eliminated by agreements for arbitration, if arbitration agreements are made valid and enforceable."). The FAA sought to promote arbitration as a benefit to commerce by making "valid, irrevocable, and enforceable" written arbitration provisions in "contract[s] evidencing transaction[s] involving commerce." 9 U.S.C. § 2.

While the FAA plainly expresses a strong federal policy favoring arbitration, there was initial uncertainty regarding the nature and scope of the Act. The early assumption was that the FAA applied only in federal courts. J.H. Cohen & K. Dayton, *The New Federal Arbitration Law*, 12 Va. L. Rev. 265, 277-278 (1926); H. Baum & L. Pressman, *The Enforcement of Commercial Arbitration Agreements in the Federal Courts*, 8 N.Y.U. L.Q. Rev. 428, 430-431, 459-460 (1930-1931). While the Act does not grant federal-question jurisdiction, federal courts applied it to state-law contract actions in diversity cases.[1] There was, however, little if any effort to apply it in state court. Baum & Pressman, 8 N.Y.U. L.Q. Rev. at 459-460.

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[1] *See, e.g., Shanferoke Coal & Supply Corp.* v. *Westchester Serv. Corp.*, 293 U.S. 449 (1935); *Krauss Bros. Lumber Co.* v. *Louis Bossert & Sons, Inc.*, 62 F.2d 1004, 1006 (2d Cir. 1933); *In re Woerner*, 31 F.2d 283, 284 (2d Cir. 1929).

Moreover, there was confusion both as to whether enforcement of arbitration provisions was a substantive or procedural requirement and whether the FAA was an exercise of Congress' Commerce Clause powers or its supposed power to prescribe general substantive law for the federal courts. *See* H.C. Strickland, *The Federal Arbitration Act's Interstate Commerce Requirement: What's Left for State Arbitration Law?*, 21 Hofstra L. Rev. 385, 391 n.33 (1992); J.F.Nooney, *Commercial Arbitration in Federal Courts*, 20 Vand. L. Rev. 607, 612 (1967); Cohen & Dayton, 12 Va. L. Rev. at 278; Baum & Pressman, 8 N.Y.U. L.Q. Rev. at 430.

The resolution of these issues became particularly significant when the Court decided *Erie R.R. Co.* v. *Tompkins*, 304 U.S. 64 (1938), requiring the application of state substantive law in diversity cases. If the FAA had constituted a congressional attempt to legislate a substantive rule of decision in diversity cases for the federal courts alone, it would have created obvious tensions with *Erie*, for *Erie* would, under those circumstances, call for state substantive arbitration laws to be applied in diversity cases. This Court resolved these and other issues concerning the scope of the Act in a series of decisions in the 1980s establishing that the FAA is, indeed, a federal substantive regulation of commerce with broad preemptive effect, applicable in *both* federal and state courts.

The contemplation-of-the-parties test under review in this case was articulated well before the Court's decisions of the 1980s. It is the product of an era when some courts remained uncertain both about the scope of the FAA and about whether to give the Act

its fullest reach into state contractual disputes. The test embodies a now thoroughly discredited view that the FAA is narrow in scope and it clashes with the FAA's sweeping federal policy in favor of arbitration.

A. The FAA Is A Commerce Clause Enactment That Reaches All Contracts Within The Scope Of Congressional Authority.

In its first post-*Erie* FAA case, the Court held that the FAA's mandate to enforce agreements to arbitrate disputes is substantive law: "[A]rbitration, whatever its merits or shortcomings, substantially affects the cause of action created by the State. The nature of the tribunal where suits are tried is an important part of the parcel of rights behind a cause of action." *Bernhardt* v. *Polygraphic Co. of Am., Inc.*, 350 U.S. 198, 203 (1956). Next, the Court made explicit that Congress enacted the FAA pursuant to "the incontestable federal foundations of 'control over interstate commerce and over admiralty.'" *Prima Paint Corp.* v. *Flood & Conklin Mfg. Co.*, 388 U.S. 395, 405 (1967) (quoting H.R. Rep. No. 96, 68th Cong., 1st Sess. 1 (1924); S. Rep. No. 536, 68th Cong., 1st Sess. 3 (1924)). *Bernhardt* and *Prima Paint* did not, however, address explicitly either the Act's application in state court or its preemptive effect.

In the 1980s, the Court addressed these issues and laid to rest any lingering doubts about the scope of the FAA. Those cases establish that the FAA "is a congressional declaration of a liberal federal policy favoring arbitration agreements, notwithstanding *any* state substantive or procedural policies to the contrary." *Moses H. Cone*, 460 U.S. at 24 (emphasis added). As an exercise of Congress' Commerce Clause powers, the substantive rules of the Act must apply

in state as well as federal courts, a fact the Court acknowledged in *Southland Corp.* v. *Keating*, 465 U.S. 1, 12 (1984). The Act embodies a strong federal policy favoring the enforcement of arbitration agreements, abrogating historic state hostility to arbitration, and superseding any contrary rule of law from either the federal courts or the states: "In creating a substantive rule applicable in state as well as federal courts, Congress intended to foreclose state legislative attempts to undercut the enforceability of arbitration agreements." *Id.* at 16.

Southland Corp. and *Perry* v. *Thomas*, 482 U.S. 483 (1987), decisively articulate the broad preemptive effect of the FAA. The Act preempts all state laws or policies that would preclude enforcement of arbitration agreements, including those laws that preclude arbitration only in a limited context. *See Southland Corp.*, 465 U.S. at 16 (FAA preempts state law precluding arbitration of disputes over franchise agreements); *Perry*, 482 U.S. at 491 (FAA preempts state law precluding arbitration of disputes over wages). "In enacting § 2 of the federal Act, Congress declared a national policy favoring arbitration and withdrew the power of the states to require a judicial forum for the resolution of claims which the contracting parties agreed to resolve by arbitration." *Southland Corp.*, 465 U.S. at 10; *Perry*, 482 U.S. at 489.

The FAA preempts not only arbitration-hostile state laws. Even the application of neutral state-law principles that affect the enforcement of arbitration provisions must be applied consistently with the federal policy. "[I]n applying general state-law principles of contract interpretation to the interpretation of an arbitration agreement within the scope of the Act, due

regard must be given to the federal policy favoring arbitration, and ambiguities as to the scope of the arbitration clause itself resolved in favor of arbitration." *Volt Information Sciences, Inc.* v. *Board of Trustees of Leland Stanford Jr. Univ.*, 489 U.S. 468, 475-476 (1989) (citation omitted). "[A]s a matter of federal law, any doubts concerning the scope of arbitrable issues should be resolved in favor of arbitration, whether the problem at hand is the construction of the contract language itself or an allegation of waiver, delay, or a like defense to arbitrability." *Moses H. Cone*, 460 U.S. at 24-25.

Taken together, the Court's decisions establish that the FAA is a broad and preemptive pronouncement of a federal requirement that all arbitration agreements within Congress' Commerce Clause authority must be enforced despite state-law rules and devices that might be utilized to defeat arbitration.

B. The Contemplation-of-the-Parties Test Is Plainly Inconsistent With This Court's FAA Decisions Of The 1980s.

The contemplation-of-the-parties test that the Alabama Supreme Court adopted in this case narrows and confuses the application of the FAA. As such, it is a remnant of a period when some courts remained uncertain of the FAA's preemptive effect, and a product of judicial hostility to arbitration.

The Alabama Supreme Court derived the contemplation-of-the-parties test from Judge Lumbard's concurring opinion in 1961 in *Metro Industrial Painting*, 287 F.2d 382. *See* Pet. App. 4a. Although Judge Lumbard recognized that the FAA applies in state as well as federal courts, he was concerned that Congress

had provided "no clear mandate . . . as to the extent to which state statutes and decisions are to be superseded." 287 F.2d at 386. He, therefore, concluded that "we must be cautious in construing the act" so as to avoid broad preemption. *Id.* His contemplation-of-the-parties test is thus an intentional narrowing of the FAA, derived not from the language or history of the Act, but from a desire to restrict preemption and from an erroneous understanding of the Act's intended reach.

Judge Lumbard proposed the rule well before this Court had established definitively in *Southland Corp.* and *Perry* the Act's broad preemptive effect. The logic of *Southland Corp.*, in particular, is fully applicable to the present case. In holding that the FAA preempts all arbitration-hostile state laws in both federal and state court, the Court explained that Congress intended directly to address "the widespread unwillingness of state courts to enforce arbitration agreements" as well as "the failure of state arbitration statutes to mandate enforcement of arbitration agreements." 465 U.S. at 13-14. The Court concluded that the FAA must be applied broadly to respond to the breadth of the problems the Act addressed: "To confine the scope of the Act to arbitrations sought to be enforced in federal courts would frustrate what we believe Congress intended to be a broad enactment appropriate in scope to meet the large problems Congress was addressing." *Id.* at 14.

The same reasoning applies here. The contemplation-of-the-parties test, by confining the FAA to a range of contracts narrower than the reach of the Commerce Clause, defeats Congress' intention to enact a broad, uniformly applicable national statute to ensure the enforceability of arbitration agreements.

The *Perry* Court subsequently reiterated that the FAA preempts all state laws that prevent enforcement of arbitration agreements, even if the laws prevent enforcement only in a limited context. The FAA, the Court explained, "embodies Congress' intent to provide for the enforcement of arbitration agreements *within the full reach of the Commerce Clause.*" 482 U.S. at 490 (emphasis added). Thus, in light of its understanding of the FAA's broad reach, *Perry* provides the answer to the question presented in this case. The Court's conclusion and reasoning make it clear that the Alabama decision below is in error.

The purpose of the contemplation-of-the-parties test is to limit the scope of the FAA. That is obvious from Judge Lumbard's opinion in *Metro Industrial* and from the Alabama Supreme Court's own justification for adopting the test. The Alabama court acknowledged explicitly in *Lopez* v. *Home Buyers Warranty Corp.*, 628 So. 2d 361 (Ala. 1993), *petition for cert. filed*, 62 U.S.L.W. 3249 (Dec. 23, 1993) (No. 93-995), that the contemplation-of-the-parties test does not further the policy behind the FAA, or even effectuate Congress' intent regarding the scope of the Act, but was adopted in Alabama precisely because it "better promotes [Alabama's] strong public policy *against* the use of predispute arbitration." *Id.* at 363 n.2 (emphasis added). The contemplation-of-the-parties test is little more than a vestige of state antipathy toward arbitration and an effort to ignore or narrow overarching federal policy.

II

NARROWING THE SCOPE OF THE FAA TO LESS THAN THE LIMITS OF FEDERAL AUTHORITY WILL EXPOSE TO HOSTILE STATE LAWS LARGE NUMBERS OF CONTRACTS WITHIN THE FEDERAL INTEREST

The FAA established a national policy ending hostility toward arbitration because Congress recognized the efficiencies to be achieved through arbitration and rejected arguments that courts provide the only forum capable of resolving disputes fairly. Nevertheless, hostility toward arbitration continues to this day in state courts and legislatures. And state court application of arbitration-hostile state laws to contracts within the federal interest continues to frustrate federal policy.

Alabama is one of three states that have declared unequivocally that their courts will not enforce arbitration agreements governed by state law. *See* Pet. App. 2a ("Predispute arbitration agreements are unenforceable under Alabama law.") (citing Ala. Code 1975, § 8-1-41); *Ex Parte Clements*, 587 So. 2d 317, 319 (Ala. 1991); *McClendon* v. *Shutt*, 115 So. 2d 740, 741 (Miss. 1959); *State* v. *Nebraska Ass'n of Public Employees*, 477 N.W.2d 577, 580 (Neb. 1991). Thus, it is consistent with Alabama policy for the Alabama Supreme Court to interpret the federal law in a manner that allows it to restrict, as sharply as possible, the enforcement of arbitration agreements. *See Lopez*, 628 So. 2d at 363 n.2.

In other states, legislatures have repealed by statute the broad common-law antagonism toward arbitration, but have retained some of this animosity by placing restrictions on arbitration agreements to which other contracts are not subject. Typical are requirements that arbitration provisions contain specific language or citations, appear in particular typeface, or in a certain place within a contract, or that the parties separately initial or sign an arbitration agreement contained in a larger contract.[2]

These mechanical requirements single out arbitration agreements for special scrutiny not imposed on other contracts, but the requirements can, at least theoretically, be met.[3] More problematic are the numerous state statutes that void absolutely any agreement to arbitrate certain types of disputes. For

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[2] *E.g.*, Md. Code Ann., Cts. & Jud. Proc. § 3-206(b) (arbitration agreement must invoke specifically the Maryland statute); Mont. Code Ann. § 27-5-114 (notice of arbitration clause must be underlined, in capital letters, and on first page of agreement); R.I. Gen. Laws § 10-3-2 (arbitration clause must be placed immediately before testimonium clause or signatures in insurance contracts); S.C. Code Ann. § 15-48-10 (notice of arbitration provision must be typed in underlined capital letters, or rubber-stamped prominently, on first page); Vt. Stat. Ann. tit. 12, § 5652(b) (arbitration clause requires exact boilerplate and must be placed prominently); Ga Code. Ann. § 9-9-2(c)(8) (party to be bound must initial arbitration clause in contract for sale or loan agreement regarding residential real estate); Tenn. Code Ann. § 29-5-302 (clause must be initialed/signed in contracts relating to farm property, structures, or goods, or residential real estate contracts); Tex. Rev. Civ. Stat. Ann. art. 224 (separate signature of parties and their lawyers required on arbitration agreement in a contract "for the acquisition by an individual person or persons . . . of real or personal property, or services, or money or credit" where total consideration is $50,000 or less).

[3] These requirements place significant burdens, however, on those doing business on a nationwide basis.

example, many state anti-arbitration laws target agreements to arbitrate insurance disputes, arbitration agreements in consumer loan and other consumer contracts, and, more generally, arbitration agreements appearing in standard form contracts, labeled contracts of "adhesion."[4] In addition, certain state courts appear willing to apply their common-law rules regarding adhesion and unconscionability in a manner particularly hostile to arbitration.[5]

The irony beneath these broader restrictions is that arbitration has its greatest social utility in precisely those contexts in which states are most likely to refuse to enforce arbitration agreements. Insurance contracts, as well as consumer loans and other consumer agreements, generally involve relatively small amounts of money. The pest control contract at issue in the present case is a good example. Such arrangements

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[4] *E.g.*, Ark. Code Ann. § 16-108-201 (insurance agreements and annuity contracts); Ga. Code Ann. § 9-9-2(c) (insurance disputes, consumer loans involving $25,000 or less, purchase of consumer goods, most consumer "acts or practices" or contracts involving consumer transactions); Ind. Code Ann. § 34-4-2-1(b) (consumer leases, sales, and loan contracts); Iowa Code Ann. § 679A.1(2) (adhesion contracts); Kan. Stat. Ann. § 5-401 (insurance contracts); Ky. Rev. Stat. Ann. § 417.050 (insurance contracts); Mo. Ann. Stat. § 435.350 (insurance contracts and contracts of adhesion); Mont. Code Ann. § 27-5-114 (contracts to acquire real/personal property, services, or money/credit where total consideration to be paid is $5,000 or less; insurance policy disputes); Ohio Rev. Code Ann. § 2711.01 (most controversies involving title to/right to possess real estate); S.C. Code Ann. § 15-48-10 (claims under insurance or annuity contracts).

[5] *See, e.g.*, *Broemmer* v. *Abortion Serv. of Phoenix, Ltd.*, 173 Ariz. 148, 840 P.2d 1013 (1992); *Patterson* v. *ITT Consumer Fin. Corp.*, 14 Cal. App. 4th 1659, 18 Cal. Rptr. 2d 563 (1993), *cert. denied*, 114 S. Ct. 1217 (1994).

are made cost-effective for the insurer, lender, or other entrepreneur—and are therefore made available at affordable prices to the consumer—by keeping down transaction and other external costs. The standard form contract is one means of making these transactions more efficient. Because small insurance and consumer transactions tend to be highly similar, the cost of reaching agreement can be reduced substantially by using experience-tested standard forms. *See Northwestern Nat'l Ins. Co.* v. *Donovan*, 916 F.2d 372, 377 (7th Cir. 1990) ("[f]orm contracts, and standard clauses in individually negotiated contracts, enable enormous savings in transaction costs"). These forms thus facilitate the high volumes of insurance and loan transactions that insurers and lenders require to generate a profit. Without standard forms, the cost of negotiating these contracts would increase the cost to consumers in the form of higher insurance premiums or less favorable lending terms, and ultimately might restrict the availability of insurance and consumer loans.

Arbitration agreements provide similar cost-saving benefits. Arbitration lowers the cost of dispute resolution. With contracts involving smaller amounts of money, the potential for costly litigation[6] may overwhelm the benefit the parties derive from the underlying transaction. The expected savings from preselected arbitration mechanisms ultimately benefit

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[6] *See, e.g.*, K. Donovan, *Bound to Arbitration? Bank Trial to Decide*, Nat'l L.J., Jan. 17, 1994, at 1 (Lawyers representing a group of plaintiffs challenging as unconscionable an arbitration clause in form loan contracts "complain that [arbitration] would deny them the discovery and threat of trial that brings about settlements.").

consumers. *Cf. Carnival Cruise Lines, Inc.* v. *Shute*, 499 U.S. 585, 594 (1991) (standard forum selection clause in cruise ship contract benefits passengers in the form of reduced fares). It is not surprising, therefore, that arbitration agreements are commonplace in insurance and loan contracts, and are particularly likely to appear in form contracts. Arbitration and the standard form are two sides of the same cost-saving coin. *Cf.* D.B. Furnish, *Commercial Arbitration Agreements and the Uniform Commercial Code*, 67 Cal. L. Rev. 317, 319 (1979) (explaining the benefits of arbitration agreements in standard form sales contracts). *See also Shearson/American Express, Inc.* v. *McMahon*, 482 U.S. 220, 225-226 (1987) and *Gilmer*, 500 U.S. at 24, in which the Court enforced arbitration agreements in form contracts.

The Congress that enacted the FAA well understood the value of arbitration to business and the consumer, value that was obvious long before the recent rampant escalation in litigation costs. *See, e.g.*, S. Rep. No. 536, 68th Cong., 1st Sess. 3 (1924) ("The settlement of disputes by arbitration appeals to big business and little business alike, to corporate interests as well as to individuals."); Joint Hearings Before the Subcommittees of the Committees on the Judiciary on S. 1005 and H.R. 646, 68th Cong., 1st Sess. 34-35 (1924) ("The evils at which arbitration agreements in general are directed are three in number. (1) The long delay usually incident to a proceeding at law .... (2) The expense of litigation. (3) The failure, through litigation, to reach a decision regarded as just . . . ."). The efficiency of arbitration is the *raison d'être* for the strong federal policy of

the FAA. Arbitration-hostile state policies are the enemies of arbitration efficiencies.

Where the FAA applies, state laws and policies hostile to arbitration are preempted and arbitration must be enforced in furtherance of federal policy. Thus, the FAA must be applied broadly, coextensively with the breadth of the federal policy favoring enforcement of arbitration agreements. The contemplation-of-the-parties test is contrary to the FAA because it narrows the scope of the Act so that the Act no longer achieves its purpose.

The contemplation-of-the-parties test is contrary to the FAA in another way. By tying the jurisdictional question of the Act's application to an inquiry into the parties' subjective intent regarding interstate activity, the test promises to generate frequent satellite litigation before the parties ever are allowed to resolve their underlying dispute. Indeed, as the Alabama Supreme Court recognized, a party to an arbitration agreement in Alabama can now demand that a court resolve the issue of the state of mind of the parties at the time they entered into the agreement. Pet. App. 4a. (quoting *Metro Indus. Painting*, 287 F.2d at 387 (Lumbard, J., concurring)). Such waste of resources is precisely what arbitration, and its enforcement through the FAA, is designed to avoid: "Contracts to arbitrate are not to be avoided by allowing one party to ignore the contract and resort to the courts. Such a course could lead to prolonged litigation, one of the very risks the parties, by contracting for arbitration, sought to eliminate." *Southland Corp.*, 465 U.S. at 7. Moreover, fact-bound inquiry into subjective intent will give virtually un-

reviewable discretion to state courts hostile to arbitration.

In any contract involving commerce in which the parties agreed to arbitrate, the federal policy behind the FAA is frustrated if the agreement is not enforced, regardless of what the parties "contemplated" regarding interstate commerce. The only limitation on the enforcement of such a strong federal policy is the limit of federal authority, not the subjective contemplation of the parties. The Court should reject the contemplation-of-the-parties test and reiterate the strong federal policy enforcing agreements to arbitrate within the full scope of congressional authority.

CONCLUSION

For the foregoing reasons, the Court should reverse the judgment of the Alabama Supreme Court.

May 19, 1994

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No. 93-1001

IN THE

Supreme Court of the United States

OCTOBER TERM, 1993

ALLIED-BRUCE TERMINIX COMPANIES, INC.
AND TERMINIX INTERNATIONAL COMPANY,

Petitioners,

v.

G. MICHAEL DOBSON, WANDA C. DOBSON
STEVEN GWIN, AND JAN GWIN,

Respondents.

On Writ of Certiorari to the Supreme Court of Alabama

BRIEF AMICUS CURIAE FOR THE AMERICAN COUNCIL OF LIFE INSURANCE IN SUPPORT OF THE PETITIONERS

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QUESTION PRESENTED

When Congress has the power, under the Commerce Clause, to regulate a transaction, but the parties did not contemplate "substantial" interstate activity when they entered into the contract for that transaction, does the contract "evidenc[e] a transaction involving commerce" within the meaning of Section 2 of the Federal Arbitration Act (9 U.S.C. § 2)?

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BRIEF AMICUS CURIAE FOR THE AMERICAN COUNCIL OF LIFE INSURANCE IN SUPPORT OF THE PETITIONERS

INTEREST OF THE AMICUS

The American Council of Life Insurance is the largest life insurance trade association in the United States, representing the interests of 640 member life insurance companies.[1] These companies currently underwrite 90.9 percent of the life insurance in force in legal reserve life insurance companies in the United States.

[1] Counsel for both the Petitioners and the Respondents have consented to the filing of this brief. Their consents are on file with the Clerk.

Ensuring that the Federal Arbitration Act is applied as broadly as possible is a matter of vital importance to the *amicus*'s members. These companies employ approximately 250,000 insurance sales representatives who have registered with the National Association of Securities Dealers ("NASD") to sell securities and, in conjunction with that registration, have agreed to arbitrate all disputes with their insurer-employers. Because of its genuine interest in promoting enforcement of arbitration agreements, therefore, the *amicus* submits this brief to offer the Court some reasons, in addition to those advanced by the Petitioners, why it should reverse the decision below.

STATUTORY PROVISIONS INVOLVED

Section 2 of the Federal Arbitration Act, 9 U.S.C. § 2 (1988), provides:

> A written provision in any maritime transaction or a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction, or the refusal to perform the whole or any part thereof, or an agreement in writing to submit to arbitration an existing controversy arising out of such a contract, transaction, or refusal, shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract.

Section 1 of the Federal Arbitration Act, 9 U.S.C. § 1 (1988), provides in pertinent part:

> . . . "commerce", as herein defined, means commerce among the several States or with foreign nations, or in any Territory of the United States or in the District of Columbia, or between any such Territory and another, or between any such Territory and any State or foreign nation, or between the District of Columbia and any State or Territory or foreign nation . . . .

STATEMENT

1. Because Petitioners set the facts forth fully in their brief, the *amicus* only summarizes the facts here. In August, 1987, respondents Steven and Jan Gwin ("the Gwins"), who owned a house in Alabama, entered into a contract with petitioner Allied-Bruce Terminix Companies, Inc. ("Terminix Service") for termite protection services ("the contract"). Appendix to Petition for Certiorari ("Pet. App."), at 1a-2a. Terminix Service is an Arkansas corporation with offices in Alabama and a number of other states. Pet. App. 2a. The contract was guaranteed by petitioner Terminix International Company ("Terminix International"), a limited partnership with its principal place of business in Tennessee. *Id*. The contract contained an arbitration clause, which provided, in pertinent part, that "any controversy or claim between [the parties] arising out of or relating to the interpretation, performance, or breach of any provision of this agreement shall be settled exclusively by arbitration." Petition for Certiorari ("Pet."), at 4.

In 1991, the Gwins sold their house to respondents G. Michael Dobson and Wanda C. Dobson ("the Dobsons"). Pet. App. 2a. The sales agreement required the Gwins to have the house inspected for termite infestation. *Id*. Terminix Service performed a visual inspection and reported that it had observed no evidence of active infestation. *Id*.

When the sale closed, the contract was transferred from the Gwins to the Dobsons. Pet. 4. After the closing, the Dobsons discovered termite damage to the house. Pet. App. 2a. The Petitioners (hereinafter "Terminix") provided repairs and further treatment in accordance with the terms of the contract. Pet. 5. Much of the material and equipment used to treat the house was purchased in other states and brought into Alabama. Pet. 5 n.6.

2. The Dobsons were not satisfied and sued Terminix in an Alabama trial court, alleging both breach of contract and claims sounding in tort. Pet. App. 2a. Relying upon the arbitration clause in the contract, Terminix moved to compel arbitration and

to stay the state court litigation. *Id.* The trial court denied that motion in a one-sentence order. Pet. App. 9a.

3. Terminix appealed the denial of its motion to the Alabama Supreme Court, which affirmed the decision of the trial court. Pet. App. 8a. The Alabama Supreme Court acknowledged that, if the Federal Arbitration Act ("FAA"), 9 U.S.C. § 1 *et seq.* (1988 & Supp. II 1990), were applicable, it would pre-empt Alabama law (which denies enforcement to pre-dispute arbitration agreements) and make the arbitration agreement enforceable. Pet. App. 2a-3a. The court further acknowledged that, if the contract in question "evidenc[ed] a transaction involving commerce" within the meaning of Section 2 of the FAA, 9 U.S.C. § 2, then the FAA would apply. Pet. App. 4a. However, it held that contracts do not "evidenc[e] a transaction involving commerce," even if the performance of those contracts actually has some nexus with interstate commerce, unless the parties, at the time that they entered into the contract, "*contemplated* substantial interstate activity." *Id.* (citation omitted). It then held that the parties to this case had not "contemplated substantial interstate activity" when they entered into the contract and that the FAA therefore did not apply. Pet. App. 4a-7a.

SUMMARY OF ARGUMENT

I. As this Court has recognized in prior decisions, Congress enacted the FAA, pursuant to its powers under the Commerce Clause of the Constitution.

The Commerce Clause authorizes Congress to regulate all activities that "affect" or otherwise have an actual nexus with interstate commerce. If the activities undertaken pursuant to a contract actually turn out to have the required nexus with interstate commerce, then Congress has the power to regulate those activities regardless of whether the contracting parties, when they entered into the contract, "contemplated" that performance of the contract would involve "substantial interstate activity."

Consequently, under the Commerce Clause, Congress may enforce agreements to arbitrate disputes in cases (such as the

present one) where the performance of the underlying contract has actually affected interstate commerce, and may do so even if one or more of the parties did not originally expect that performance of the contract would involve substantial interstate activity.

II. For the foregoing reasons, the holding of the court below amounts to a finding that, in enacting Section 2 of the FAA, Congress chose not to exercise all of the powers available to it under the Commerce Clause. However, both the plain language of the FAA and its underlying purposes, as identified in prior decisions of this Court, indicate that Congress did intend the FAA to reach all transactions within the scope of congressional authority under the Commerce Clause.

Certainly, the plain language of the FAA does not limit its reach in the manner suggested by the court below. By its terms, the FAA applies to both pre-dispute and post-dispute agreements to arbitrate controversies arising out of "a contract evidencing a transaction involving commerce." Thus, if one were to interpret this phrase as including only those contracts where the parties contemplated substantial interstate activity at the time of contracting, then the enforceability of agreements to arbitrate *existing* disputes, made long after the parties had entered into the underlying contract, would depend not on what the parties knew when they agreed to arbitration, but on what they expected when entering into the underlying contract. It is difficult to imagine why Congress would mandate such an illogical result.

Moreover, as this Court has held in prior decisions, Congress' purpose in enacting the FAA was to pre-empt state law that disfavored arbitration agreements and to ensure that such agreements were enforced according to their terms. Naturally, then, Congress would want to pre-empt such state law as far as the Commerce Clause would permit. The only conceivable reason for Congress to limit the application of Section 2 (and thus the FAA) to cases in which the contracting parties contemplated substantial interstate activity would be to prevent unfair surprise by application of the FAA where the parties did not expect it. But there was no reason for Congress to worry about anyone

being unfairly "surprised" by application of the FAA when, as this Court has held, the FAA merely effectuates the intentions of the parties by enforcing their own agreements to arbitrate.

ARGUMENT

I. CONGRESS IS NOT LIMITED, UNDER THE COMMERCE CLAUSE, TO REGULATING ONLY THOSE TRANSACTIONS WHERE THE CONTRACTING PARTIES ORIGINALLY CONTEMPLATED SUBSTANTIAL INTERSTATE ACTIVITY

It is well established that "[t]he Federal Arbitration Act rests on the authority of Congress to enact substantive rules under the Commerce Clause." *Southland Corp. v. Keating*, 465 U.S. 1, 11 (1984); *Perry v. Thomas*, 482 U.S. 483, 489 (1987).[2] And it has long been recognized that, under the Commerce Clause, Congress may regulate activities that actually affect interstate commerce. It does not matter, for purposes of the Commerce Clause, whether the parties to an arbitration agreement believed, when entering into the underlying contract, that the performance of the contract would involve "substantial interstate activity." What matters is whether, in retrospect, the activities undertaken pursuant to the contract actually had the required nexus with interstate commerce.

"No all-embracing definition [of interstate commerce] has ever been formulated." *Carter v. Carter Coal Co.*, 298 U.S. 238, 298 (1936). However, it is well established, and has long been recognized by this Court, that Congress' powers under the Commerce Clause are very broad and that "the commerce power extends not only to 'the use of channels of interstate or foreign commerce,' and to 'protection of the instrumentalities of interstate commerce . . . or persons or things in commerce,' but also to 'activities affecting commerce.'" *Hodel v. Virginia Surface*

[2] The Commerce Clause provides that Congress has the power "[t]o regulate commerce with foreign nations, and among the several States, and with the Indian tribes." U.S. Const. art. I, § 8, cl. 3.

Mining & Reclamation Ass'n, 452 U.S. 264, 276-277 (1981) (quoting *Perez v. United States*, 402 U.S. 146, 150 (1971)). *See also Fry v. United States*, 421 U.S. 542, 547 (1975) (under the Commerce Clause, Congress may regulate even transactions that, when viewed in isolation, are of a "purely intrastate" nature, if "the activity, combined with like conduct by others similarly situated, affects commerce among the States"); *Katzenbach v. McClung*, 379 U.S. 294, 305 (1964) ("The power of Congress in this field [interstate commerce] is broad and sweeping; where it keeps within its sphere and violates no express constitutional limitation it has been the rule of this Court, going back almost to the founding days of the Republic, not to interfere"); *United States v. Wrightwood Dairy Co.*, 315 U.S. 110, 119 (1942) ("The commerce power . . . extends to those activities intrastate which so affect interstate commerce, or the exertion of the power of Congress over it, as to make regulation of them appropriate means to . . . the effective exertion of the granted power to regulate interstate commerce").[3]

Obviously, then, the performance of a contract may have the required nexus with interstate commerce, even if it does not actually involve "substantial interstate activity." Therefore, it can hardly be necessary, for the Commerce Clause to apply, that the contracting parties have *foreseen* such activity. Indeed, this Court has never held, as far as the *amicus* can determine, that

[3] Certainly, based on the facts of the present case, there can be no question that Terminix, in performing its contractual obligations, engaged in the kind of activities that Congress may regulate under the Commerce Clause. Terminix has offices and does business in a number of states. Pet. App. 2a. Moreover, in performing its obligations under the contract at issue, Terminix used materials and equipment that were purchased in other states and then brought into Alabama. Pet. 5 n.6. As this Court has held, "[n]o commercial enterprise of any kind which conducts its activities across state lines has been held to be wholly beyond the regulatory power of Congress under the Commerce Clause." *United States v. South-Eastern Underwriters Ass'n.*, 322 U.S. 533, 553 (1944).

notwithstanding any actual nexus with interstate commerce, Congress' authority under the Commerce Clause is limited to only those transactions where the parties, at the time of contracting, believed that the transaction would involve "substantial interstate activity."

Moreover, prior holdings of this Court as to the scope of the FAA strongly suggest that the Court does not view the applicability of the Commerce Clause as being dependent upon the original intentions of the parties. In interpreting the language of the FAA, the Court has determined whether contracts "evidenc[ed] a transaction involving commerce" by looking at whether the performance of those contracts, *in retrospect*, actually had some nexus with interstate commerce. *See Wilko v. Swan*, 346 U.S. 427, 428-430, 432 (1953) (the underlying contract evidenced a transaction in interstate commerce "in the light of the complaint" subsequently filed by one of the contracting parties, which alleged that it had been defrauded "through the instrumentalities of interstate commerce"), *overruled on other grounds*, *Rodriguez de Quijas v. Shearson/American Express, Inc.*, 490 U.S. 477 (1989); *Bernhardt v. Polygraphic Co. of America*, 350 U.S. 198, 200-201 (1956) (an employment contract did not evidence a transaction involving commerce because, *inter alia*, the employee did not show that, in performing his duties under the contract, he had "engag[ed] in activity that affected commerce, within the meaning of our decisions") (footnote omitted).

II. IN ENACTING SECTION 2 OF THE FEDERAL ARBITRATION ACT, CONGRESS INTENDED TO EXERCISE THE FULL SCOPE OF ITS POWERS UNDER THE COMMERCE CLAUSE

The holding of the court below amounts to a finding that, in enacting Section 2 of the FAA, Congress chose to exercise only a portion of the powers granted to it by the Commerce Clause. However, neither the language of Section 2, nor Congress' purposes in enacting it, supports the conclusion that Congress intended to exercise less than its full powers under the Commerce

Clause. Indeed, although this Court has never specifically addressed the issue before it today -- the meaning of the FAA's phrase "a contract evidencing a transaction involving commerce" -- it has indicated that Congress intended to exercise its full powers under the Commerce Clause in enacting the FAA. *See Perry v. Thomas*, 482 U.S. at 490 ("the Federal Arbitration Act . . . embodies Congress' intent to provide for the enforcement of arbitration agreements *within the full reach of the Commerce Clause*") (emphasis added); *Southland Corp.*, 465 U.S. at 14 (Congress would only "need to call on the Commerce Clause if it intended the Act to apply in state courts. . . . We therefore view the 'involving commerce' requirement in § 2, not as an inexplicable limitation on the power of federal courts, but as a *necessary* qualification on a statute intended to apply in state and federal courts") (emphasis added)[4]; *Wilko v. Swan*, 346 U.S. at 438 ("Congress has afforded participants *in transactions subject to its legislative power* an opportunity generally to secure prompt, economical, and adequate solution of controversies through arbitration . . . .") (emphasis added).

A. The Plain Language Of Section 2 Does Not Limit The Reach Of The FAA To Transactions In Which The Contracting Parties Originally Contemplated Substantial Interstate Activity

Section 2 of the FAA provides that:

> A written provision in any maritime transaction or a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction, or the refusal to perform the whole or any part thereof, or an agreement in writing to submit to arbitration an existing controversy arising out of

---

[4] Although it was "necessary" for Congress, if it wished to have the FAA apply in state courts, to limit the reach of the FAA to the scope of congressional powers under the Commerce Clause, it would not be "necessary" for Congress to further limit the reach of the FAA in the manner claimed by the court below.

> such a contract, transaction, or refusal, shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or equity for the revocation of any contract.

9 U.S.C. § 2. "Commerce," in turn, is defined as:

> commerce among the several States or with foreign nations, or in any Territory of the United States or in the District of Columbia, or between any such Territory and another, or between any such Territory and any State or foreign nation, or between the District of Columbia and any State or Territory or foreign nation . . . .

9 U.S.C. § 1.

Certainly, there is nothing in the language of the statute itself that requires the contracting parties to have contemplated "substantial" interstate activity at the time of contracting. Nor, as discussed above in Part I of the Argument, has the Commerce Clause ever been held to require such a limitation.

Moreover, interpreting the phrase "a contract evidencing a transaction involving interstate commerce" in the manner espoused by the court below produces an illogical result when that interpretation is applied to other parts of Section 2. Section 2 provides, in part, for the enforcement of agreements to arbitrate that are made only *after* a dispute has arisen between parties to an underlying contract -- namely, "agreement[s] in writing to submit to arbitration an existing controversy arising out of such a contract . . . ." 9 U.S.C. § 2 (emphasis added). It is clear, from context, that the words "such a contract" refer to "a contract evidencing a transaction involving commerce." Thus, if the court below were correct that a contract did not "evidenc[e] a transaction involving commerce" unless the parties had contemplated substantial interstate activity at the time of contracting, then the enforceability of post-dispute agreements to arbitrate would depend upon what the parties expected at the time that they entered into the underlying contract -- not when they agreed to arbitrate. It is difficult to imagine why Congress would refuse to enforce a post-dispute arbitration agreement, even if the parties

made it with full knowledge that the performance of the underlying contract had involved interstate activity, simply because at some earlier time, when they entered into the underlying contract, they did not expect that its performance would involve such activity.

B. In View Of The Purposes Behind Section 2, It Would Make No Sense To Limit The Reach Of The FAA To Transactions In Which The Contracting Parties Originally Contemplated Substantial Interstate Activity

Even if this Court were to decide that the language of Section 2 is not in itself dispositive, the purposes behind the passage of the FAA, as identified in past decisions of this Court, indicate that Congress intended to exercise the full scope of its powers under the Commerce Clause.

In enacting the FAA, Congress declared a strong federal policy favoring the enforcement of arbitration agreements and pre-empted attempts by states, like Alabama, to disfavor such agreements. As the Court held in *Southland Corp.*:

> In enacting § 2 of the [F]ederal [Arbitration] Act, Congress declared a national policy favoring arbitration and withdrew the power of the states to require a judicial forum for the resolution of claims which the contracting parties agreed to resolve by arbitration.
>
> * * *
>
> In creating a substantive rule applicable in state as well as federal courts, Congress intended to foreclose state legislative attempts to undercut the enforceability of arbitration agreements.

465 U.S. at 10, 16 (footnotes omitted). *See also Moses H. Cone Memorial Hosp. v. Mercury Construction Corp.*, 460 U.S. 1, 24 (1983) ("Section 2 is a congressional declaration of a liberal federal policy favoring arbitration agreements, notwithstanding any state substantive or procedural policies to the contrary"). Given Congress' desire to override state laws that "undercut the enforceability of arbitration agreements," it would naturally want

to pre-empt such laws to the maximum extent that it could -- namely, to the maximum extent permitted by the Commerce Clause. The only conceivable reason for Congress to limit the application of Section 2 (and thus the FAA) to cases in which the contracting parties contemplated substantial interstate activity would be to prevent unfair surprise by application of the FAA where the parties had no reason to expect it. But there was no reason for Congress to worry about anyone being unfairly "surprised" by application of the FAA when, as this Court has repeatedly pointed out, the FAA merely effectuates the intentions of the parties by enforcing their own agreements to arbitrate. *See, e.g., Volt Information Sciences, Inc. v. Board of Trustees*, 489 U.S. 468, 478-479 (1989) (the FAA was designed, above all, to "ensur[e] that private agreements to arbitrate are enforced according to their terms"); *Dean Witter Reynolds v. Byrd*, 470 U.S. 213, 221 (1985) ("[t]he preeminent concern of Congress in passing the Act was to enforce private agreements into which parties had entered . . . ."); *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 625 (1985) ("[t]he 'liberal federal policy favoring arbitration agreements' manifested by this provision [Section 2] and the Act as a whole, is at bottom a policy guaranteeing the enforcement of private contractual arrangements . . . .") (citation omitted).

CONCLUSION

The holding of the court below imposes an arbitrary and unwarranted limitation on the reach of the FAA -- a limitation that finds no support either in the Commerce Clause or in the FAA itself. That holding, if permitted to stand, would allow states like Alabama to frustrate the strong federal policy favoring arbitration agreements and would thwart the reasonable expectations of both individuals and businesses, including life insurance companies, that their agreements to arbitrate will be enforced. Therefore, the judgment below should be reversed.

Respectfully submitted,

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INTEREST OF *AMICI*

The undersigned *amici curiae*, the Attorneys General of Alabama and of nineteen other States, submit this brief in support of respondents G. Michael Dobson and Wanda C. Dobson.

As constitutional officers of the States they represent, *amici* have the responsibility to defend the vital interests of federalism at issue in this case. *Amici* submit that the Federal Arbitration Act ("FAA") creates binding uniform law only in the *federal* courts. The instant case arose in the *state* courts of Alabama. To apply the Act to proceedings in state court, as petitioners seek to do, would fly in the face of fundamental principles of state sovereignty.

SUMMARY OF ARGUMENT

Until this Court's decision in *Southland Corp. v. Keating*, 465 U.S. 1 (1984), this Court had never countenanced the application of the Federal Arbitration Act in state court proceedings. Indeed, after the passage of the Act in 1925, lower courts and commentators were unanimous in their conclusion that the FAA did *not* apply to state courts.

In *Southland*, this Court extended the FAA to cover state court proceedings, in a majority opinion written by Chief Justice Burger and joined by Justices Brennan, White, Marshall, Blackmun, and Powell. But this Court was denied the benefit of adversarial briefing on the matter. The appellees in *Southland* erroneously assumed that the Act governs proceedings in state court, based on dictum in this Court's decision in *Moses H. Cone Memorial Hospital v. Mercury Construction Corp.*, 460 U.S. 1 (1983), and appellees conceded the point in their brief.[1] Yet *Moses H. Cone* was a diversity action that did not arise in state court and therefore could not have decided the issue. The issue was raised in *Southland* only briefly in oral argument, largely because "the parties stipulated in the court below that . . . the

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[1] *See* Brief of Appellees in No. 82-500 (filed June 6, 1983) at 25 n.30; *Keating v. Superior Court*, 31 Cal.3d 584, 604, 645 P.2d 1192, 1203, 183 Cal. Rptr. 360, 371-72 (1982).

federal Act applied."[2] Because the questions presented in *Southland* did not explicitly identify the Act's application to state court as the issue to be decided by this Court,[3] *amici* were not put on notice and consequently did not participate.

But the institutional interests of the States — and, indeed, of the entire system of federalism — cannot be waived by a private litigant. Justice O'Connor's dissent in *Southland*, 465 U.S. at 21-36, in which the current Chief Justice joined, is demonstrably correct and should be adopted by this Court as the proper interpretation of the FAA. Justice O'Connor explained that the text and structure of the Act clearly indicate that it does not apply to proceedings in state court, and she exposed the fundamental defects in the majority's reasoning.[4]

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[2] Tr. Oral Arg. in No. 82-500, at 6 (quoting counsel for appellants). One Justice asked, "Do you think [Congress] intended the Federal Arbitration Act to apply to state courts at all?," *id.* at 7, and told *counsel for appellants*, Southland, et al., that "the evidence of what Congress intended is pretty clearly against you." *Id.* at 8. Counsel for appellants responded by asserting that *Moses H. Cone* "specifically held" that the FAA governed proceedings in state court." *Id.* at 7. Under questioning, counsel was forced to akcknowledge that the comment in *Moses H. Cone* was only dictum. *Id.* at 7-8.

[3] This Court framed the questions presented as:

> (a) whether the California Franchise Investment Law, which invalidates certain arbitration agreements covered by the Federal Arbitration Act, violates the Supremacy Clause and (b) whether arbitration under the federal Act is impaired when a class-action structure is imposed on the process by the state courts.

465 U.S. at 3.

[4] Writing separately, Justice Stevens agreed that — as enacted in 1925 — the FAA did not apply to state court proceedings and that "the 1925 Congress that enacted the statute viewed the statute as essentially procedural in nature." 465 U.S. at 17 (opinion concurring in part and dissenting in part). But he believed that the meaning of the law had somehow changed over time: "I am persuaded that the intervening developments in the law compel the conclusion that the Court has reached." *Id.*

Subsequently, Justice Stevens stated more critically that, "[e]ven though the Arbitration Act had been on the books for almost 50 years in 1973, apparently neither the Court nor the litigants even considered the possibility that the Act had pre-empted state-created rights. It is only in the last few years that the Court has effectively rewritten the statute to give it a pre-emptive scope that Congress certainly did not intend." *Perry v. Thomas*, 482 U.S. 483, 493 (1987) (Stevens, J., dissenting).

This case is ultimately more about federalism than about arbitration. *Amici* submit that each State is entitled to decide for itself how to govern proceedings in its own courts. Most of the States have chosen to facilitate arbitration. But the FAA should not be read to compel them to do so. "The essence of federalism is that States must be free to develop a variety of solutions to problems and not be forced into a common, uniform mold." *Addington v. Texas*, 441 U.S. 418, 431 (1979). The role of States as laboratories of democracy, *New State Ice Co. v. Liebman*, 285 U.S. 262, 311 (1932) (Brandeis, J., dissenting), is especially salient here. It was, after all, the New York arbitration statute that served as the model for the federal Act, and it was the explicit intent of the FAA's drafters to permit each State to adopt its own arbitration policy according to its own unique circumstances and interests.

We recognize that statutory interpretations should not be discarded lightly. But *Southland's* extension of the FAA to state courts was rendered without briefing based on an imprudent concession by a private litigant, is demonstrably incorrect, and is in tension with important principles of judicial restraint and federalism, as reflected in such recent decisions in *O'Melveny & Myers v. FDIC*, No. 93-489 (June 13, 1994), *New York v. United States*, 112 S. Ct. 2408 (1992), *Gregory v. Ashcroft*, 111 S. Ct. 2395 (1991), and *Will v. Michigan Dept. of State Police*, 491 U.S. 58 (1989). Subsequent decisions involving the FAA, such as *Volt Information Sciences, Inc. v. Board of Trustees of Leland Stanford Junior University*, 489 U.S. 468, 477 n.6 (1989) (permitting parties contractually to agree to adopt state procedural rules of arbitration and reserving the question whether FAA §§ 3 and 4 are applicable in state court), have also undercut the logic of *Southland*.[5]

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[5] *See, e.g., Comment, The Federal Arbitration Act: Conflicting Interpretations of its Scope*, 61 U. Cin. L. Rev. 623, 646 (1992) ("The *[Volt]*

The failure of Congress to override *Southland* by legislation cannot be treated as decisive.[6] This Court has been willing to overturn judicial decisions interpreting statutes where the "development of the law," including "the growth of judicial doctrine," has "removed or weakened the conceptual underpinnings from the prior decision." *Patterson v. McLean Credit Union*, 491 U.S. 164, 173 (1989). "[W]here the later law has rendered the decision irreconcilable with competing legal doctrines or policies, the Court has not hesitated to overrule an earlier decision." *Id.* (citations omitted). *See, e.g., Director, OWCP v. Greenwich Collieries*, 62 U.S.L.W. 4543 (June 20, 1994) (overruling interpretation of § 7(c) of Administrative Procedure Act set forth in *NLRB v. Transportation Management Corp.*, 462 U.S. 393 (1984)); *McDermott International, Inc. v. Wilander*, 498 U.S. 337, 348-55 (1991) (overruling prior decisions construing the Jones Act).[7]

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majority's hostility toward the application of section 3 and 4 to state court proceedings is a direct pronouncement of the principles which Justice O'Connor and Chief Justice Rehnquist dissented against in the *Southland* decision."); Wallace, *Securities Arbitration After McMahon, Rodriguez, and the New Rules: Can Investors' Rights Really be Protected*, 43 Vand. L. Rev. 1199, 1213 (1990) (analyzing *Volt* as a victory for values of federalism).

[6] As this Court explained in *Boys Markets, Inc. v. Retail Clerks*, 398 U.S. 235 (1970) (overruling prior precedent in order to protect state court jurisdiction):

> Nor can we agree that conclusive weight should be accorded to the failure of Congress to respond to [a prior decision] on the theory that congressional silence should be interpreted as acceptance of the decision. The Court has cautioned that "it is at best treacherous to find in congressional silence alone the adoption of a controlling rule of law."

Id. at 241 (citation omitted); *see also Brecht v. Abrahamson*, 113 S. Ct. 1710, 1719 (1993).

[7] In *Rodriguez de Quijas v. Shearson/American Express, Inc.*, 490 U.S. 477, 479-86 (1989), this Court was willing to overrule *Wilko v. Swan*, 346 U.S. 427 (1953), and thereby to overturn an interpretation of the Securities Act, 15 U.S.C. § 77n, that had stood for 36 years. Obviously, there could be no principled basis for adopting a different rule for decisions like *Southland* simply because they favored arbitration.

Amici therefore submit that *Southland* should be overruled insofar as it held that the FAA governs proceedings in state court.[8]

I. THE FEDERAL ARBITRATION ACT DOES NOT GOVERN PROCEEDINGS IN STATE COURT

The text and structure of the Federal Arbitration Act clearly indicate that it does not apply to proceedings in state court. Section 2 provides that a written arbitration agreement "shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract." 9 U.S.C. § 2. Section 2 does not, on its face, identify which judicial forums are bound by its requirements or

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[8] Given that one Alabama decision has already been vacated in light of *Southland*, *see York Int'l v. Alabama Oxygen Co.*, 465 U.S. 1016 (1984), the Alabama courts since the decision in *Southland* have assumed that the FAA applies in state courts. *E.g., Ex Parte Alabama Oxygen Co.*, 452 So.2d 860 (Ala. 1984). But this assumption surely cannot prevent the States now appearing as *amici* from raising the issue. The question of whether *Southland* should be overruled is logically intertwined with (indeed, antecedent to) the question on which the Court granted *certiorari*: whether § 2 of the Arbitration Act requires reversal of the judgment of the Alabama Supreme Court. If the Act does not apply to state courts at all, the judgment below must be affirmed. Once a federal question is before the Court, the parties "are not confined . . . to the same arguments which were presented in the courts below." *Dewey v. Des Moines*, 173 U.S. 193, 198 (1899); *see also Illinois v. Gates*, 462 U.S. 213, 248 (1983) (White, J., concurring) (there is no requirement that "all arguments on behalf of, let alone in opposition to, a federal claim be raised and decided below"); *United States National Bank of Oregon v. Independent Insurance Agents of America, Inc.*, 113 S. Ct. 2173, 2178 (1993) (noting that court of appeals could decide case on issue raised by neither party).

In any event, the States are appearing as *amici* in *support* of the judgment below. It is well settled that a prevailing party or its *amici* may invoke alternative grounds for affirming a judgment and therefore may "assert in a reviewing court any ground in support of [the] judgment, whether or not that ground was relied upon or even considered by the trial court." *Dandridge v. Williams*, 397 U.S. 471, 475-76 n.6 (1970).

what procedures govern its enforcement. The FAA deals with these matters in §§ 3 and 4. These implementing provisions expressly apply only to the federal courts. Section 3 provides:

> If any suit or proceeding be brought in any *of the courts of the United States* upon any issue referable to arbitration . . . the court . . . shall on application of one of the parties stay the trial of the action until such arbitration has been had in accordance with the terms of the agreement . . . .

9 U.S.C. § 3 (emphasis added). Section 4 specifies that a party aggrieved by another's refusal to arbitrate

> may petition any *United States district court* which, save for such agreement, would have jurisdiction under title 28, in a civil action or in admiralty of the subject matter . . . for an order directing that such arbitration proceed in the manner provided for in such agreement . . . .

9 U.S.C. § 4 (emphasis added). Section 9, which addresses the enforcement of antitrust awards, is also relevant. It provides that, "[i]f no court is specified in the agreement of the parties, then such application may be made to *the United States court* in and for the district within which such award was made." 9 U.S.C. § 9 (emphasis added).

This Court has already held that "[s]ections 1, 2 and 3 are integral parts of a whole" and that they must be read as coextensive in scope. *Bernhardt v. Polygraph Co. of America*, 350 U.S. 198, 201 (1956). The Act's implementing provisions thus provide clear evidence that § 2 extends only to federal courts.

The only textual analysis by the *Southland* majority was its contention that, if "Congress sought only to create a procedural remedy in the federal courts, there can be no explanation for the express limitation in the Arbitration Act to contracts 'involving commerce.'" *Id.* at 14. But this assertion does not prove the point.

Initially, the *Southland* majority's argument ignores the fact that Congress had powerful reasons for restricting the scope of the Act to merchants involved in commerce, so that the FAA would not extend to *every* contract (including contracts of unsuspecting consumers) in *every* case in federal court.

Moreover, even if the reference to commerce, and hence to Congress' powers under Art. I, § 8, cl. 3, was intended to provide an alternative constitutional foundation for the Act, that does not mean that the FAA should be read to govern state-court proceedings. After all, in *Prima Paint v. Flood & Conklin*, 388 U.S. 395, 404-05 (1967), this Court used the reference to commerce to conclude that the FAA could be applied in federal court diversity cases consistent with *Erie R. Co. v. Tompkins*, 304 U.S. 64 (1938),[9] yet in *Prima Paint* this Court quite deliberately did *not* hold that the FAA governs proceedings in state court. *See infra* p. 17. As Justice O'Connor has noted, "it is enough to recognize that Congress relied *at least in part* on its Article III power over the jurisdiction of the federal courts." *Southland Corp.*, 465 U.S. at 28 n.14 (dissenting opinion). For example, several rules of judicial procedure contain references to subject matters over which Congress possesses legislative authority, such as commerce and maritime affairs, yet there has never been any suggestion that these rules apply in state courts. *See id.* at 26 n.11.

In fact, the curious aspect of § 2 is not the reference to "commerce." It is instead the undisputed fact that the FAA does not create a substantive right enforceable in federal court under the jurisdictional grant of 28 U.S.C. § 1331. *See Southland*, 465 U.S. at 15-16 n.9. This result is indeed "anomal[ous]," *Moses H. Cone Hospital*, 460 U.S. at 25 n.32, and indicates that the FAA was intended only as a procedural statute that does not govern proceedings in state courts. *See Southland*, 465 U.S. at 30 n.19 (O'Connor, J., dissenting). However, following *Southland's* directive that "the Arbitration Act 'creates a body of federal substantive law'" that "requir[es] the parties to honor

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[9] *See Bernhardt v. Polygraphic Co.*, 350 U.S. 198, 208 (1956) (Frankfurter, J., concurring).

arbitration agreements" and governs "the underlying issue of arbitrability," 465 U.S. at 12, 15 n.9 (citation omitted), courts have begun to fashion what is essentially a federal common law of arbitration agreements,[10] purportedly under the auspices of a statute that — while denominated "substantive" — does not in fact create federal subject-matter jurisdiction. This state of affairs is assuredly beyond what Congress authorized, *see* pp. 11-16, *infra*, and raises troubling Article III issues. *See, e.g., O'Melveny & Myers v. FDIC*, No. 93-489 (June 13, 1994).

For all these reasons, the facial silence of § 2 of the FAA should not be taken as a license to declare that state courts as well as federal courts must apply § 2 — particularly in light of the powerful interests of federalism at issue here. Even in ordinary pre-emption cases, federal law cannot be held to displace state law in the absence of a clear congressional statement. *See, e.g., English v. General Electric*, 496 U.S. 72, 82 (1990); *Silkwood v. Kerr-McGee Corp.*, 464 U.S. 238, 256 (1984). This requirement is heightened in areas of traditional state concern, such as the enforcement of contracts and the protection of consumers, where this Court has always "start[ed] with the assumption that the historic police powers of the States were not to be superseded by the federal act unless that was the clear and manifest purpose of Congress." *Rice v. Santa Fe Elevator Corp.*, 331 U.S. 218, 230 (1947). In the context of the FAA, this Court has already held that "[t]he FAA contains no express pre-emptive provision, nor does it reflect a congressional intent to occupy the entire field of arbitration." *Volt Information Sciences, Inc.*, 489 U.S. at 477.

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[10] *See* Hirshman, *The Second Arbitration Trilogy: The Federalization of Arbitration Law*, 71 Va. L. Rev. 1305, 1347 (1985) (concluding, in light of this Court's decisions, that "the FAA embodies a federal policy favoring arbitration that is not confined to the express language of the Act. . . . [F]ederal courts may decide issues not expressly covered by the FAA by crafting a federal common law rule even if the otherwise applicable state law does not discriminate against arbitration."); Strickland, *The Federal Arbitration Act's Interstate Commerce Requirement: What's Left for State Arbitration Law?*, 21 Hofstra L. Rev. 385, 387 (1992) (observing that this Court's decisions, including *Southland*, "articulate a federal common law of arbitration that replaces state law whenever the FAA is applicable").

Although this Court has recognized that the Constitution protects state sovereignty and imposes substantive limits on congressional power, *see, e.g., New York v. United States*, 112 S. Ct. 2408, 2420 (1992), this Court has emphasized that the primary protections for the States lie in the structure of government as a whole and especially in the political branches. *See Garcia v. San Antonio Metropolitan Transit Auth.*, 469 U.S. 528, 551 (1985). This Court has therefore held that, "if Congress intends to alter the 'usual constitutional balance between the States and the Federal Government,' it must make its intention to do so 'unmistakably clear in the language of the statute.'" *Will v. Michigan Dept. of State Police*, 491 U.S. 58, 65 (1989) (citation omitted). Only a crystal-clear statement of congressional intent can put the States on notice of the impending displacement of state law and interference with state functions, and thus enable the political safeguards of federalism to function. "'[T]o give the state-displacing weight of federal law to mere congressional *ambiguity* would evade the very procedure for lawmaking on which *Garcia* relied to protect states' interests.'" *Gregory v. Ashcroft*, 111 S. Ct. 2395, 2403 (1991) (quoting L. Tribe, American Constitutional Law § 6-25, p. 480 (2d ed. 1988)).

Where federal law purports to regulate the operation of state courts, the need for a clear statement of congressional intent is at its zenith. The control over state court dockets, including the right to a civil jury trial in the state courts, is not governed by the federal Constitution, but is a matter solely of state law and state concern. As Justice Frankfurter observed, "the States are as free from control by Congress in establishing state systems for litigation as is Congress free from state control in establishing a federal system for litigation." *Brown v. Gerdes*, 321 U.S. 178, 188 (1944) (concurring opinion).[11] "The general rule 'bottomed

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[11] *See generally Atlantic Coast Line R.R. v. Brotherhood of Locomotive Eng'rs*, 398 U.S. 281, 285, 287 (1970) (stating that "[o]ne of the reserved powers [under the Constitution] was the maintenance of state judicial systems for the decision of legal controversies" and referring to the "fundamental constitutional independence of the States and their courts"); *Fay v. Noia*, 372

deeply in belief in the importance of state control of state judicial procedure, is that federal law takes the state courts as it finds them.'" *Howlett v. Rose*, 496 U.S. 356, 371 (1990) (quoting Hart, *The Relations Between State and Federal Law*, 54 Colum. L. Rev. 489, 508 (1954), and citing Justice O'Connor's dissent in *Southland Corp. v. Keating*).

Indeed, the choice of forum to adjudicate state-created rights is generally not subject to Congress' power to regulate at all. Thus, in *Northern Pipeline Co. v. Marathon Pipe Line*, 458 U.S. 50 (1982), this Court invalidated Congress' grant of authority to bankruptcy courts to hear claims arising under state law. A plurality explained that congressional power to intrude upon the province of the constitutional courts is at "a minimum" when it seeks "to control the manner in which [a right under state law] is adjudicated." *Id.* at 84.[12]

The decision in *Southland* threatens complete denial of access to state courts for adjudication of state-created rights whenever a business corporation chooses to insert an arbitration provision in "a contract evidencing a transaction involving commerce." This far-reaching result, which would dramatically alter the balance between federal and state judicial systems,

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U.S. 391, 466-67 (1963) (Harlan, J., dissenting) ("The right of the State to regulate its own procedures governing the conduct of litigants in its courts, and its interest in supervision of those procedures, stand on the same constitutional plane as its right and interest in framing 'substantive' laws governing other aspects of the conduct of those within its borders."); *Baltimore & O.R. Co. v. Baugh*, 149 U.S. 368, 401 (1893) ("[T]he Constitution of the United States . . . recognizes and preserves the autonomy and independence of the States — independence in their legislative and . . . in their judicial departments. . . . Any interference with either . . . is an invasion of the authority or the State and, to that extent, a denial of its independence.").

[12] The constitutional question cannot be avoided by reference to the parties' agreement. States that choose to make certain disputes nonarbitrable define the cause of action in advance to survive any attempt to waive the parties' right to litigate in court. The parties' agreement by itself could not override this exercise of state police power. Only the imprimatur of Congress could render the agreement preemptive of the legislative choice of forum.

should not be permitted to stand in the absence of unambiguous congressional intent. The FAA contains no evidence of such intent.

II. *SOUTHLAND CORP. v. KEATING* SHOULD BE OVERRULED

The majority in *Southland Corp. v. Keating* did not address, let alone dispute, most of the foregoing analysis of the text and structure of the FAA. Instead, the majority opinion by Chief Justice Burger relied on three highly dubious propositions (*see* 465 U.S. at 11-16) to determine that the FAA governs proceedings in state court. The majority believed: **1)** that its interpretation of the Act was ordained by the legislative history of the Federal Arbitration Act; **2)** that such a result was compelled by *Prima Paint v. Flood & Conklin*, 388 U.S. 395 (1967); and **3)** that such a result was required by pragmatic considerations, such as the need to avoid forum shopping. Each of these propositions is incorrect.

1. The majority in *Southland Corp. v. Keating* asserted that, "*[a]lthough the legislative history is not without ambiguities*, there are strong indications that Congress had in mind something more than making arbitration agreements enforceable only in the federal courts." 465 U.S. at 12 (emphasis added). This lukewarm conclusion should not be enough to outweigh the contrary implication of the statute's text and structure. Moreover, the legislative history proves precisely the opposite of what the *Southland* majority believed. As Justice O'Connor has observed, "[o]ne rarely finds a legislative history as unambiguous as the FAA's. That history establishes conclusively that the 1925 Congress viewed the FAA as a procedural statute, applicable only in federal courts, derived, Congress believed, largely from the federal power to control the jurisdiction of the federal courts." 465 U.S. at 25 (dissenting opinion).

Prior to 1925, the federal courts, applying general federal common law pursuant to *Swift v. Tyson*, 16 Pet. 1 (1842), generally refused in diversity cases to enforce arbitration laws

that had been adopted by several major commercial States.[13] Even if the federal courts were inclined to enforce the clauses, there was no procedure by which they could do so. Cohen and Dayton, *The New Federal Arbitration Law*, 12 Va. L. Rev. 265, 275-76 (1926).

The Federal Arbitration Act was drafted by the American Bar Association's Committee on Commerce, Trade and Commercial Law to remedy this situation. It was enacted by Congress in 1925 pursuant to its constitutional powers under the Commerce Clause, Admiralty Clause, and Article III. There was no need to regulate the States, because the problem lay in the application by *federal courts* of general federal common law. Moreover, because arbitration "has long been considered procedural,"[14] Congress quite naturally did not view the FAA as creating a substantive rule of law applicable in state court.

A principal author of the Act, Julius Cohen of the American Bar Association, wrote at the time,

> [T]he statute as drawn establishes a *procedure in the Federal courts* for the enforcement of certain arbitration agreements. It is no infringement upon *the right of each state to decide for itself what contracts shall or shall not exist under its laws*. . . . [W]hether or not an arbitration agreement is to be enforced is a question of the law of *procedure* and is determined by the law of the jurisdiction wherein the remedy is sought.[15]

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[13] *See, e.g., Atlantic Fruit Co. v. Red Cross Line*, 276 F. 319 (S.D.N.Y. 1921), *aff'd*, 5 F.2d 218 (2d Cir. 1924); *Lappe v. Wilcox*, 14 F.2d 861 (N.D.N.Y. 1926).

[14] 5 Moore, Federal Practice 128 (2d ed. 1948); *see also Heckers v. Fowler*, 2 Wall. 123, 128 (1864) (upholding reference of case to arbitrator as a procedural act); *Marine Transit Corp. v. Dreyfus*, 284 U.S. 263, 278 (1932) (upholding application of Arbitration Act to admiralty cases as a matter of "procedure").

[15] Cohen & Dayton, *The New Federal Arbitration Law*, 12 Va. L. Rev., at 275-276 (emphasis added).

Mr. Cohen told congressional subcommittees that "[t]he theory on which you do this is that you have the right to tell the federal court how to proceed."[16] He rejected any suggestion that the Act would affect state courts:

> Nor can it be said that the Congress of the United States, *directing its own courts* . . ., would infringe upon the provinces or prerogatives of the States. . . . [T]he question of enforcement relates to the law of remedies and *not to substantive law*. The rule must be changed for the jurisdiction in which the agreement is sought to be enforced. . . . There is no disposition therefore by means of the Federal bludgeon to force an individual State in.o an unwilling submission to arbitration enforcement.[17]

The House Report on the FAA stated that "[w]hether an agreement for arbitration shall be enforced or not is a question of procedure," not substance, and explained that "[t]he bill declares that such agreements shall be recognized and enforced *by the Courts of the United States*." H.R. Rep. No. 96, 68th

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[16] Arbitration of Interstate Commercial Disputes, Joint Hearings on S. 1005 and H.R. 646 Before the Subcomms. of the Comms. on the Judiciary, 68th Cong., 1st Sess. 17 (1924) ("Joint Hearings"); *see also id.* at 38 ("The primary purpose of the statute is to make enforcible [sic] in the Federal courts such agreements for arbitration.") (statement of Mr. Cohen); Sales and Contracts to Sell in Interstate and Foreign Commerce, and Federal Commercial Arbitration, Hearing on S. 4213 and S. 4214 before a Subcommittee of the Senate Committee on the Judiciary, 67th Cong., 4th Sess., 2 (1923) ("Senate Hearing") ("This bill follows the lines of the New York arbitration law, applying it to the fields wherein there is Federal jurisdiction"); Committee on Commerce, Trade and Commercial Law, *The United States Arbitration Act and Its Application*, 11 A.B.A.J. 153, 156 (1925) ("[The FAA] rests upon the constitutional provision by which Congress is authorized to establish and control inferior Federal courts. So far as congressional acts relate to the procedure in the Federal courts, they are clearly within the congressional power").

[17] Joint Hearings at 39-40 (emphasis added).

Cong., 1st Sess. 1 (1924) (emphasis added).[18] The drafting committee itself noted that the "statute providing for the enforcement of arbitration agreements does *relate solely to procedure of the Federal courts*. It is no infringement upon the right of each state to decide for itself what contract shall or shall not exist." Committee on Commerce, Trade and Commercial Law, *The United States Arbitration Act and Its Application*, 11 A.B.A.J. 153, 154-155 (1925) (emphasis added). In explaining the bill in the House of Representatives, Representative Graham assured his fellow Members of Congress that:

> This bill . . . does not involve any new principle of law except to provide a simple method by which the parties may be brought before the court in order to give enforcement to that to which they have already agreed. . . . It creates no new legislation, grants no new rights, except a remedy to enforce an agreement in commercial contracts and in admiralty contracts.

65 Cong. Rec. 1,931 (1924).

Contemporary commentators recognized that the Act did not impose any restrictions on the States.[19] One scholar has

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[18] To similar effect, the Senate Report noted that the New York statute, after which the FAA was patterned, had been upheld against constitutional attack the previous year in *Red Cross Line v. Atlantic Fruit Co.*, 264 U.S. 109 (1924). S. Rep. No. 536, 68th Cong., 1st Sess., 3 (1924). In *Red Cross*, Justice Brandeis based the Court's approval of the New York statute on the fact that the statute effected no change in the substantive law.

[19] The A.B.A. Committee that drafted the legislation wrote: "So far as the present law declares simply the policy of recognizing and enforcing arbitration agreements in the Federal courts it does not encroach upon the province of the individual states." Committee on Commerce, Trade and Commercial Law, 11 A.B.A.J. at 155. *See also* Cohen & Dayton, *The New Federal Arbitration Law*, 12 Va. L. Rev. at 276-77; Baum & Pressman, *The Enforcement of Commercial Arbitration Agreements in the Federal Courts*, 8 N. Y. U. L. Q. Rev. 428, 459 (1931). Williston wrote: "Inasmuch as arbitration acts are deemed procedural, the United States Act applies only to the federal courts." 6 S. Williston & G. Thompson, The Law of Contracts 5368 (rev. ed. 1938).

noted that, "[f]or years, courts and commentators agreed that the statute applied only in the federal courts and so governed only the few contract suits that happened to involve diversity or admiralty jurisdiction." Hirshman, *The Second Arbitration Trilogy: The Federalization of Arbitration Law*, 71 Va. L. Rev. 1305, 1305 (1985) (citing cases).[20]

More recent students of the FAA uniformly and emphatically reach the same conclusion. *Prima Paint*, 388 U.S. at 424 (Black, J., dissenting); Stipanowich, *Punitive Damages in Arbitration*, 66 B.U. L. Rev. 953, 972 n.110 (1986) ("the legislative history and contemporary writings do tend to confirm that Congress originally intended the Federal Arbitration Act as a set of procedural rules for federal courts"); Note, *The Consequences of a Broad Arbitration Clause Under the Federal Arbitration Act*, 52 B.U. L. Rev. 571, 578 (1972) ("The proponents of the Act viewed it as procedural in nature, enacted under the power of Congress to regulate the federal courts and consequently only applicable in the federal courts"); Note, *Scope of the United States Arbitration Act in Commercial Arbitration: Problems in Federalism*, 58 Nw. U. L. Rev. 468, 492 (1963) ("there is no legislative history to support a conclusion that Congress intended to make the act applicable in state courts"); Note, 73 Harv. L. Rev. 1382, 1383 (1960) ("the House committee report indicated that the act was to apply only in the federal system. . . . [Congress manifested] the understanding that the act was to regulate procedure in the federal courts"); Note, *Erie, Bernhardt, and Section 2 of the United States Arbitration Act: A Farrago of Rights, Remedies, and a Right to a Remedy*, 69 Yale L. J. 847, 863 (1960) (noting "the complete absence of congressional intent to make the federal act applicable to state court actions").

[20] Until *Southland*, many courts continued to hold that the FAA did not govern proceedings in state court. In *Ex parte Alabama Oxygen Co.*, 433 So. 2d 1158 (Ala. 1983), for example, the Alabama supreme court ruled that the FAA did not bind the States. After this Court vacated and remanded for reconsideration in light of *Southland*, *see York Int'l v. Alabama Oxygen Co.*, 465 U.S. 1016 (1984), the Alabama court simply deferred to this Court's mandate. *See Ex parte Alabama Oxygen Co.*, 452 So. 2d 860 (Ala. 1984). *See also Barron v. Tastee Freez Intern., Inc.*, 482 F. Supp. 1213, 1217 (E.D. Wisc. 1980) (assuming that the Federal Arbitration Act applied only to federal courts and stating, in adjudicating the enforceability of an arbitration clause in a diversity action, that a federal court was not required to consider any contrary state policy and might well reach a different result than a state court faced with the same issue); *Bache Halsey Stuart Shields, Inc. v. Moebius*, 531 F. Supp. 75, 77 (E.D. Wisc. 1982) (same); *Sandefer v. Reynolds Securities Inc.*, 618 P.2d 690, 691 (Colo. App. 1980) (holding state securities law claim

It was not until 35 years after passage of the Act that some judges developed the concept that there were certain substantive aspects to the FAA applicable in state as well as federal courts. *Robert Lawrence Co. v. Devonshire Fabrics, Inc.*, 271 F.2d 402 (2d Cir. 1959), *cert. dismissed*, 364 U.S. 801 (1960). This suggestion stemmed from a fear that the *Erie* doctrine would prohibit the federal courts from applying the Act in diversity cases, *id.* at 404-09 — a fear that was later put to rest in *Prima Paint*. Even after the *Erie* concern surfaced, one of the judges who decided *Robert Lawrence* counseled caution because of the important state sovereignty interests at stake:

> [T]he legislative history of the Arbitration Act of 1925 reveals little awareness on the part of Congress that state law might be affected. . . . Having no clear mandate from Congress as to the extent to which state statutes and decisions are to be superseded, we must be cautious in construing the act lest we excessively encroach on the powers which Congressional policy, if not the Constitution, would reserve to the states.

Metro Industrial Painting Corp. v. Terminal Constr. Co., 287 F.2d 382, 386 (2d Cir.) (Lumbard, C.J., concurring), *cert. denied*, 368 U.S. 817 (1961).

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not arbitrable); *Pullman, Inc. v. Phoenix Steel Corp.*, 304 A.2d 334, 338 (Del. Super. Ct. 1973) (holding FAA inapplicable in state court); *Hilton Construction Co. v. Martin Mechanical Contractors, Inc.*, 303 S.E.2d 119, 123 (Ga. App.) (holding FAA inapplicable in state court and noting that "the all inclusive aspects of the Act are directed only to the federal courts"), *aff'd*, 308 S.E.2d 830 (Ga. 1983); *Kress Corp. v. Edward C. Levy Co.*, 430 N.E.2d 593, 595-96 (Ill. App. 1981) (reading *Prima Paint* as holding merely that "Federal courts [should] apply the Federal act" and concluding that the FAA does not govern proceedings in state court); *Downing v. Allstate Insurance Co.*, 335 N.W.2d 139, 142 (Mich. App. 1983) (Kelly, J., concurring) ("I find the federal arbitration act wholly inapplicable to these state court proceedings"); *Thayer v. American Financial Advisers, Inc.*, 322 N.W.2d 599, 603 (Minn. 1982) (holding FAA inapplicable in state court).

2. In *Prima Paint*, a diversity action, this Court deliberately declined to hold that the Act applied in any respect in the state courts. The *Prima Paint* Court was asked to hold, based on the reasoning of *Robert Lawrence*,[21] that the Federal Arbitration Act applies in state courts and that it is a national substantive law. The Court refused to do so, stating that "the question is whether Congress may prescribe how *federal courts* are to conduct themselves with respect to subject matter over which Congress plainly has power to legislate. The answer to that can only be in the affirmative." 388 U.S. at 405 (emphasis added). One Justice was willing to adopt wholesale the Second Circuit's more broadly written opinion. *See* 388 U.S. at 407 (Harlan, J., concurring).

But the majority opinion in *Prima Paint* "carefully avoided any explicit endorsement of the view that the Arbitration Act embodied substantive policies that were to be applied to all contracts within its scope, whether sued in state or federal courts." P. Bator, D. Meltzer, P. Mishkin & D. Shapiro, Hart and Wechsler's The Federal Courts and the Federal System 810 (3d ed. 1988). Justice Black took pains to point out:

> The Court here does not hold . . . that the body of federal substantive law created by federal judges under the Arbitration Act is required to be applied by state courts. A holding to that effect — which the Court seems to leave up in the air — would flout the intention of the framers of the Act.

388 U.S. at 424 (dissenting opinion). Nothing in the *Prima Paint* majority opinion contradicts this statement. *Prima Paint* thus provides no support for the holding in *Southland Corp. v. Keating*, and the *Southland* majority's reliance on *Prima Paint* was entirely unjustified.

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[21] In *Robert Lawrence*, the Second Circuit had announced — in dictum — that the FAA was "a declaration of national law equally applicable in state or federal courts." 271 F.2d at 407.

3. Finally, the *Southland* Court relied on pragmatic considerations, primarily the supposed danger of forum shopping, to conclude that § 2 of the FAA creates a substantive rule of law applicable to state as well as federal courts. *See* 465 U.S. at 15-16. But the Court's reasoning was persuasively rebutted by Justice O'Connor:

> In controversies involving incomplete diversity of citizenship, there is simply no access to federal court and therefore no possibility of forum shopping. In controversies *with* complete diversity of citizenship the FAA grants federal-court access equally to both parties; no party can gain any advantage by forum shopping. Even when the party resisting arbitration initiates an action in state court, the opposing party can invoke FAA § 4 and promptly secure a federal-court order to compel arbitration.

465 U.S. at 34 (dissenting opinion). Justice O'Connor might have added that, if forum shopping were truly a serious danger, it is difficult to understand why it had not surfaced during the first 60 years of the Act's existence.

Ironically, the FAA was adopted to *cure* the problem of forum shopping created by federal courts' application of general federal common law in diversity cases.[22] The drafters of the FAA might have addressed the matter by requiring federal courts sitting in diversity to follow the arbitration law of the State in which they sat. However, the statute's framers deliberately chose a different approach. They decided to adopt a uniform federal law that would make arbitration agreements enforceable even in federal courts located in States that had no arbitration

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[22] *See* Joint Hearings at 16 (statement of Julius Cohen of the American Bar Association); Senate Hearing at 2; Cohen & Dayton, *The New Federal Arbitration Law*, 12 Va. L. Rev., at 275-76; Sturges & Murphy, *Some Confusing Matters Relating to Arbitration Under the United States Arbitration Act*, 17 Law & Contemp. Prob. 580, 590 (1952).

law.[23] And, instead of "bludgeon[ing] States into compliance" with the new federal law, *Southland*, 465 U.S. at 34 (dissenting opinion), the FAA's drafters opted to press for passage of coordinated state legislation applicable in state court. Accordingly, the key language of the Uniform Act for Commercial Arbitration is identical to that of § 2 of the FAA.[24]

A total of 45 States have now enacted modern statutes to facilitate arbitration, with 34 States and the District of Columbia adopting the Uniform Act. *See* 7 U.L.A. 1 (Supp. 1993). Many States, however, have chosen to adopt statutory exclusions to protect consumers and others of unequal bargaining power or information.[25] Of course, *Southland* effectively nullifies the power of state courts to give effect to such exclusions.

In sum, if there is a danger of forum shopping, it is one accepted by the framers of the FAA and one that they have addressed with a carefully devised plan — a plan that this Court obliterated in *Southland* with its extravagant reading of the Act.

CONCLUSION

For all of the foregoing reasons, *Southland Corp. v. Keating* should be overruled insofar as it extended the FAA to state court proceedings, and the judgment below should be affirmed.

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[23] *See, e.g.*, Joint Hearings at 35.

[24] *See* 47 A.B.A. Rep. 318 (1922); Joint Hearings at 28.

[25] Variations include statutory exclusions as to medical malpractice, *e.g.*, Alaska Statutes § 09.55.535, Ga. Stat. §9-9-2(c)(1); contracts involving consumers, *e.g.*, Ga. Stat. § 9-9-2(c)(5), (6), (7), Mont. Code Ann. § 27-5-114(2)(b); employer-employee disputes, *e.g.*, Ky. Revised Stat. § 417.050, La. Revised Stat. § 9:4216, Ann. Code of Md. § 3-206(b), N.C. Gen. Stat. § 1-567.2(b)(2), Tex. Rev. Civ. Stat. Ann. art. 224, West Va. Stat. § 55-10-1; torts, *e.g.*, Ark. Code Ann. § 16-108-201, Ga. Stat. § 9-9-2(c)(10), Iowa Code Ann. § 697A.1(2)(c), Mont. Code Ann. § 27-5-114(2)(a); uninsured motorists, doctors and lawyers, *e.g.*, 14 Me. Revised Stat. § 5948, S.C. Code § 15-48-10; and contracts of adhesion, *e.g.*, Iowa Code Ann. § 697A.1(2)(a).

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July 18, 1994

No. 93-1001

JUN 9 1994

IN THE

Supreme Court of the United States

October Term, 1993

[redacted] CLEVELAND CHEMICAL COMPANIES, INC., and [redacted] MINING INTERNATIONAL COMPANY,

Petitioners,

v.

[redacted] WANDA C. DOBSON, [redacted] GWEN and [redacted] GWEN,

Respondents.

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INTEREST OF *AMICUS CURIAE*

Amicus curiae, the Southern Poverty Law Center, submits this brief in support of respondents G. Michael Dobson and Wanda C. Dobson.[1]

The Southern Poverty Law Center is a non-profit legal and educational organization dedicated to protecting the rights of poor people and minorities. *Amicus* has an interest in this case because it is committed to ensuring that consumers are not unfairly deprived of a judicial forum in which to resolve their legal claims.

Arbitration clauses are essentially waivers of the traditional right to jury trial. Waivers of such rights should never be lightly presumed, particularly in situations where there is a marked imbalance in knowledge and power. But many consumer situations are characterized by precisely such imbalances. Accordingly, *amicus* urges this Court to clarify that the Federal Arbitration Act ("FAA") does not encompass all contracts within Congress' constitutional authority to regulate and that, in particular, it does not govern arbitration agreements in consumer contracts and other transactions in which reasonable persons in the parties' positions at the time of contracting would not have contemplated substantial interstate activity in carrying out the terms of the contract.

SUMMARY OF ARGUMENT

The salient language of § 2 of the Federal Arbitration Act, 9 U.S.C. § 2, is the phrase "contract evidencing a transaction involving commerce." Petitioners urge that this phrase be read as extending the Act to the full extent of Congress' power under the Commerce Clause, Art. I, § 8, cl. 3. But, unlike statutes in which Congress itself has defined the specific persons and activities that affect commerce, the FAA requires courts to determine in each instance whether a particular contract

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[1] Letters reflecting written consent of the parties to the submission of this brief have been filed with the Clerk of the Court.

"evidences a transaction involving commerce." It is therefore implausible to think that Congress meant to include within the scope of the FAA *all* contracts within its constitutional power to regulate — *i.e.*, all contracts. Had Congress meant to do so, it would have specified that the Act applied to "all contracts affecting commerce," or simply "all contracts."

Amicus submits that Congress' intent is best effectuated by an objective version of the "contemplation of the parties" test followed by courts for over thirty years since it was first suggested by Judge Lumbard in *Metro Indus. Painting Corp. v. Terminal Const. Co.*, 287 F.2d 382, 387 (2d Cir.) (Lumbard, C.J., concurring), *cert. denied*, 368 U.S. 817 (1961). At least 16 courts have followed the reasoning of Judge Lumbard's thoughtful concurring opinion. *See* Strickland, *The Federal Arbitration Act's Interstate Commerce Requirement: What's Left for State Arbitration Law?*, 21 Hofstra L. Rev. 385, 418 & 421 nn. 197-200 (1992) (citing cases). If *stare decisis* is to be recognized in the context of judicial interpretations of statutes, then Congress' failure since 1961 to displace the "contemplation of the parties" test must be accorded weight.

Moreover, in recent times the commerce power has come to be virtually without limit. Thus, Congress can regulate a farmer's production of wheat for home consumption. *Wickard v. Filburn*, 317 U.S. 111, 117-18 (1942). It can criminalize neighborhood loanshark agreements. *Perez v. United States*, 402 U.S. 146 (1971).[2] It can prohibit even local restaurants from engaging in racial discrimination. *Katzenbach v. McClung*, 379 U.S. 294 (1964).

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[2] In *Perez*, this Court explained that, even if there is no "proof that the particular intrastate activity against which a sanction was laid had an effect on commerce," the sanction is nevertheless permissible if the intrastate activity falls within "a class of activities . . . properly regulated by Congress," and that, "[w]here the class of activities is regulated and that class is within the reach of federal power, the courts have no power 'to excise, as trivial, individual instances' of the class." 402 U.S. at 152, 154 (citation omitted).

We have no quarrel with the contemporary expansion of Congress' authority under the Commerce Clause.[3] But precisely because of the extent of that power, petitioners' reading of the Arbitration Act would sweep virtually *all* agreements into the Act. Federal law would suddenly guarantee doctors the statutory right to insert arbitration clauses into forms signed by their patients, requiring them to waive a judicial forum for any malpractice claims. Federal law would similarly guarantee landlords, television repair shops, dry cleaners, and every other local business the right — regardless of their highly attenuated connection to interstate commerce — to insert clauses into their form contracts waiving consumers' rights to a judicial forum. Indeed, in this very case, petitioners insist that a homeowner's contract for termite control services is itself regulable as interstate commerce. If even such local and traditionally intrastate activities are within the Arbitration Act, it is hard to see what is excluded.

Congress never intended the Federal Arbitration Act to be given such an unlimited reading. Indeed, Congress was repeatedly assured by the Act's drafters that it would *not* have such a far-reaching and illogical result.

States have made deliberate decisions to exempt many kinds of consumer transactions from their arbitration statutes. Under petitioners' construction of the Act, these carefully crafted systems for consumer protection would be obliterated in one fell swoop. Given the potential for dramatic intrusion into areas of traditional state concern, petitioners' interpretation of the FAA could not be adopted unless it were supported by a crystal clear statement of congressional intent. *See Gregory v. Ashcroft*, 111 S. Ct. 2395, 2401-03 (1991). If anything, however, it is plain that Congress deliberately *rejected* petitioners' construction of the FAA.

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[3] However, we note that some Justices have expressed concern about the contemporary scope of the Commerce Clause. *See, e.g., Hodel v. Virginia Surface Mining & Reclamation Ass'n*, 452 U.S. 264, 310-12 (1981) (Rehnquist, now C.J., concurring in the judgment).

In the end, the arguments of petitioners and their *amici* rest more on current policy trends in favor of arbitration than on the text and history of the statute. But such arguments are a patently insufficient basis for rewriting a 60-year-old statute. Moreover, the recent decisions of this Court favoring arbitration have involved businesses and other sophisticated parties, not ordinary consumers. *E.g.*, *Shearson/American Express Inc. v. McMahon*, 482 U.S. 220 (1987) (Securities Exchange Act of 1934 and RICO claims); *Rodriguez de Quijas v. Shearson/ American Express, Inc.*, 490 U.S. 477 (1989) (Securities Act of 1933).

For all these reasons, the judgment below should be affirmed.

I. THE FEDERAL ARBITRATION ACT WAS NEVER INTENDED TO GO TO THE LIMITS OF CONGRESS' COMMERCE POWER

The Federal Arbitration Act was never intended to alter the historic power of the States to protect their citizens and consumers against the forced surrender of their traditional rights to trial by jury. The Act was never intended to go to the limits of congressional authority under the Commerce Clause.

(1) The framers of the FAA expected the Act to apply solely to ordinary contract disputes "between merchants." Cohen & Dayton, *The New Federal Arbitration Law*, 12 Va. L. Rev. 265, 281 (1926). The Act was drafted by a committee of the American Bar Association, acting upon instructions to consider and report upon "the further extension of the principle of *commercial arbitration*." Report of the Forty-Third Annual Meeting of the A.B.A., 45 A.B.A. Rep. 75 (1920) (emphasis added). The chairman of the ABA committee that drafted the bill testified before the Senate Judiciary Subcommittee that the FAA was "'purely an act to give the merchants the right or the privilege of sitting down and agreeing with each other as to what their damages are, if they want to do it. Now that is all there is in this.'" Hearing on S. 4213 and S. 4214 before a Subcommittee of the Senate Committee on the Judiciary, 67th Cong., 4th Sess. 9 (1923), *quoted in Gilmer v. Interstate/*

Johnson Lane Corp., 500 U.S. 20, 39 (1991) (Stevens, J., dissenting).[4]

There is no evidence in the lengthy legislative history to the Arbitration Act that Congress contemplated that the Act would apply to consumer contracts. On the contrary, the history reveals that the Act "was written with the implicit assumption that it would be invoked by commercial actors having relatively equal bargaining power." Stempel, *A Better Approach to Arbitrability*, 65 Tul. L. Rev. 1377, 1380 (1991). The organizations that sponsored the FAA were chambers of commerce, shippers, large agricultural producers, and other prominent business groups whose members were engaged in

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[4] *E.g.*, *Sales and Contracts to Sell in Interstate and Foreign Commerce, and Federal Commercial Arbitration, Hearings Before a Subcommittee of the Committee on the Judiciary on S. 4213 and S. 4214*, 67th Cong., 4th Sess. 2 (1923) (statement of Charles L. Bernheimer, chairman of the arbitration committee of the New York Chamber of Commerce) ("[t]he adoption of . . . the Federal statute and the uniform State statute will . . . enable business men to settle their disputes expeditiously and economically"); *id.* at 8 (statement of W.H. Piatt, Chairman of the Committee of Commerce, Trade and Commercial Law of the American Bar Association) ("there does seem to be quite a demand in commercial centers on the part of a good many commercial organizations . . . to have the privilege of having a vehicle constructed to effectuate an agreement to arbitrate"); *Arbitration of Interstate Commercial Disputes, Joint Hearings on S. 1005 and H.R. 646 before the Subcommittees of the Committees on the Judiciary*, 68th Cong., 1st Sess. 7 (1924) ("The Chairman. What you have in mind is that this proposed legislation relates to contracts arising in interstate commerce. Mr. Bernheimer. Yes; entirely. The farmer who will sell his carload of potatoes, from Wyoming, to a dealer in the State of New Jersey, for instance."); *id.* at 27 (statement of Alexander Rose, representing the Arbitration Society of America) ("We have a weakness in our system of arbitration. We need, and we must have the cooperation of the Federal courts. We must have the cooperation of the Federal statute, because while the dispute is a domestic one, we can well dispose of it. But when a merchant in New York sells his merchandise to some one in a foreign jurisdiction, his arbitration law is defeated . . . ."); *id.* at 41 ("If business men desire to submit their disputes to speedy and expert decision, why should they not be enabled to do so?") (statement of Julius Cohen).

interstate commerce on a national scale.[5]

(2) The text of the statute refers neither to "all" contracts nor to all contracts "affecting" commerce. Instead, the salient text of the Act limits its scope to "contract[s] evidencing a transaction involving commerce." 9 U.S.C. § 2. The words of the statute cannot be ignored. The Arbitration Act is quite unlike most laws regulating interstate commerce, which do not require case-by-case analysis as to whether a given activity bears a sufficiently close connection to interstate commerce as to fall within the statute. Most laws simply regulate the chosen activity directly. *See, e.g., Perez v. United States*, 402 U.S. 146 (1971); *Katzenbach v. McClung*, 379 U.S. 294 (1964). Such a "jurisdictional inquiry . . ., turning as it does on the circumstances presented in each case and requiring a particularized judicial determination, differs significantly from that required when Congress itself has defined the specific persons and activities that affect commerce and therefore require federal regulation." *Gulf Oil Corp. v. Copp Paving Co.*, 419 U.S. 186, 197 n.12 (1974); *see also Summit Health, Ltd. v. Pinhas*, 111 S. Ct. 1842, 1849-51 (1991) (Scalia, J., joined by O'Connor, Kennedy, and Souter, JJ., dissenting).[6]

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[5] *Arbitration of Interstate Commercial Disputes, Joint Hearings on S. 1005 and H.R. 646 before the Subcommittees of the Committees on the Judiciary*, 68th Cong., 1st Sess. 7 (1924) (statement of Charles L. Bernheimer, chairman of the arbitration committee of the New York Chamber of Commerce) ("The statement I make is backed up by 73 commercial organizations in this country.").

[6] The American Arbitration Association suggests that this Court overlook "the particular words that Congress used" in "any particular statute" in determining the statute's scope. Br. *Amicus Curiae* at 12-13. This novel approach to statutory interpretation is as self-evidently flawed as is the Association's argument that the FAA should be interpreted as if it were the Sherman Act. *Id.* at 13-14. The statutes' texts are completely different, and "[t]he floor debates on the Sherman Act reveal, in Senator Sherman's words, an intent to 'g[o] as far as the Constitution permits Congress to go.'" *Summit Health, Ltd. v. Pinhas*, 111 S. Ct. at 1846 n.7 (quoting 20 Cong. Rec. 1167 (1889)). The legislative history of the FAA points to a contrary conclusion.

The test established by Congress requires courts to judge whether a particular contract evidences a "*transaction involving commerce.*"[7] Because a contract is simply the written memorialization of the intentions of the parties entering the contract, those intentions are of utmost importance in determining whether a contract evidences a transaction involving interstate commerce. The contemplation test should be an objective, not subjective, inquiry that looks to the face of a contract and, if necessary, to the circumstances of the contract's formation and performance for evidence of a transaction involving interstate commerce. The contemplation test, in its objective form, focuses on the expectations of reasonable persons in the parties' positions at the time they entered into the contract. As in any situation in which a court determines the reasonable expectations of the parties, evidence of subjective intent is not irrelevant, but it is likewise not controlling. *See, e.g., C.P. Robinson Constr. Co. v. National Corp. for Hous. Partnerships*, 375 F. Supp. 446, 450 (M.D.N.C. 1974) (the "subjective intent of the parties is not controlling in determining if the agreement objectively evidences a transaction involving commerce, but it is illuminating as to how the parties interpreted their own contract").[8]

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[7] Petitioners argue that § 2 requires only that a contract provide evidence of a transaction, not evidence that the transaction involves interstate commerce. Brief for Petitioners at 15. But the clear meaning of § 2 is that a contract must provide evidence of a transaction that will involve commerce. "[I]nvolving commerce" is an adjectival phrase describing the transaction to be evidenced. The phrase "a transaction involving commerce" carries the same meaning as "a commerce-involving transaction."

[8] The American Bankers Association claims that the contemplation of the parties test is "an anachronism" that is at odds with contemporary business needs. ABA Br. 2. But it is surely illegitimate for this Court to discard longstanding statutory interpretations simply on the allegation that they have become inconvenient. Congress is free to revise the FAA if necessary. In any event, Judge Lumbard's concern was not to restrict unduly the reach of the FAA, but rather to define its reach properly, consistent with the requirements of the statute's text. Judge Lumbard's exposition of the contemplation test was explicitly premised on his appreciation of the "broad remedial purpose" of the FAA. *Metro Indus. Painting Corp.*, 287 F.2d at 387.

The contemplation test as described by the Supreme Court of Alabama asks whether there is objective evidence that the parties contemplated *substantial* interstate activity. This requirement is not designed to apply the FAA stingily only to those transactions involving unusually large levels of interstate activity; rather the use of the word "substantial" suggests that a contract does not "evidenc[e] a transaction involving commerce" when the transaction will relate to interstate commerce in only a tangential, *de minimis* manner. For example, the parties might well assume, in entering a contract, that a local termite service will use vehicles that consume gasoline refined out-of-state, but such an effect on interstate commerce should hardly be considered "substantial." Similarly, as Judge Lumbard explained, "[t]he fact that it is necessary for one party to cross state lines in order to fulfill obligations arising out of the contract should not by itself bring the arbitration clause within the reach of the federal statute. The [FAA] should apply only when the parties know or have reason to believe that the performance of the contract will require *substantial* interstate movement." *Metro Indus. Painting Corp.*, 287 F.2d at 388 (concurring opinion) (emphasis added). Decisions in Alabama make clear that the requirement of "substantiality" is a proper element of the standard.[9]

The contemplation test has been adopted by at least 16 courts.[10] It strikes a reasonable balance: by honoring the

[9] *See, e.g., Ex parte Lorance*, 632 So.2d 475 (Ala. 1994); *Henderson v. Superior Ins. Co.*, 628 So.2d 365, 367-68 (Ala. 1993); *First Real Estate Corp. of Alabama v. Brown Marx Tower Limited Partnership*, 620 So.2d 648, 649 (Ala. 1993).

[10] *E.g., Litton RCS, Inc. v. Pennsylvania Turnpike Comm'n*, 376 F. Supp. 579, 585-87 (E.D. Pa. 1974), *aff'd*, 511 F.2d 1394 (3d Cir. 1975); *Monte v. Southern Delaware County Auth.*, 212 F. Supp. 604, 609-11 (E.D. Pa.), *rev'd*, 321 F.2d 870 (3d Cir. 1963); *Varley v. Tarrytown Assoc., Inc.*, 477 F.2d 208, 209 (2d Cir. 1973); *Singer Co. v. Tappan Co.*, 403 F. Supp. 322, 323 n.1 (D.N.J. 1975), *aff'd*, 544 F.2d 513 (3d Cir. 1976); *O'Meara v. Texas Gas Transmission Corp.*, 230 F. Supp. 788, 790-91 (N.D. Ill. 1964); *Ex parte Clements*, 587 So. 2d 317, 319 (Ala. 1991); *Ex parte Warren*, 548 So. 2d 157, 159-60 (Ala.), *cert. denied*, 493 U.S. 998 (1989); *Action CATV, Inc. v.*

reasonable expectations of the parties, it ensures the enforceability of arbitration agreements involving national businesses obviously engaged in interstate commerce, while preserving an enclave for consumer contracts and local transactions that should not be subject to the FAA.

By contrast, petitioners' test reduces predictability and encourages forum shopping. If the FAA were interpreted to cover any contract whose performance turns out to affect interstate commerce, then the parties will not necessarily know in advance whether the FAA will apply to their transaction. If two persons enter a contract that includes an arbitration agreement but contains no indication whatsoever that the contract involves interstate commerce, either party, under petitioners' theory, could bring the contract under the coverage of the FAA by choosing to perform in a manner that involves interstate commerce — even if the connection to interstate commerce is wholly gratuitous and unexpected. This would enable one party to frustrate the intentions of the other, who may have been unwilling to enter an agreement that would be covered by the procedures of the FAA. Such a result would be inimical to Congress' aim of respecting the parties' reasonable expectations. *See Volt Information Sciences v. Board of Trustees of Leland Stanford Jr. Univ.*, 489 U.S. 468, 479 (1989) ("it does not follow that the FAA prevents the enforcement of agreements to arbitrate under different rules than those set forth in the Act itself. Indeed, such a result would be quite inimical to the FAA's primary purpose of ensuring that private agreements to

Wildwood Partners, Ltd., 508 So. 2d 1274, 1276 (Fla. Dist. Ct. App. 1987); *Riverfront Properties Ltd. v. Max Factor III*, 460 So. 2d 948, 953 (Fla. Dist. Ct. App. 1984); *University Casework Sys., Inc. v. Bahre*, 362 N.E.2d 155, 162 (Ind. Ct. App. 1977); *Pathman Constr. Co. v. Knox County Hosp. Ass'n*, 326 N.E.2d 844, 852 (Ind. Ct. App. 1975); *R.J. Palmer Constr. Co. v. Wichita Band Instrument Co.*, 642 P.2d 127, 130 (Kan. Ct. App. 1982); *Paramore v. Inter-Regional Fin. Group Leasing Co.*, 316 S.E.2d 90, 92 (N.C. App. 1984); *Cohoon v. Ziman*, 298 S.E.2d 729, 730-31 (N.C. App. 1983); *Burke County Pub. Schs. Bd. of Educ. v. Shaver Partnership*, 279 S.E.2d 816, 822 (N.C. App. 1981); *Deep South Oil Co. v. Texas Gas Corp.*, 328 S.W.2d 897, 905-06 (Tex. Civ. App. 1959).

arbitrate are enforced according to their terms. Arbitration under the Act is a matter of consent, not coercion, and parties are generally free to structure their arbitration agreements as they see fit.").

(3) This Court's prior decisions support the contemplation test and are inconsistent with petitioners' reading of the Act. In *Bernhardt v. Polygraphic Co. of America*, 350 U.S. 198 (1956), this Court indicated that the "involving commerce" language in the FAA applies to those who are employed in commerce, rather than consumers or ordinary employees. This Court stated that the contract at issue (a plant superintendent's employment contract signed in New York and performed in Vermont) did not

> evidence "a transaction involving commerce" within the meaning of § 2 of the Act. There is no showing that petitioner while performing his duties under the employment contract was working "in" commerce, was producing goods for commerce, or was engaging in activity that affected commerce, within the meaning of our decisions.

Id. at 200-01. Quite plainly, however, the employment contract would have been within Congress' constitutional authority to regulate. Thus, *Bernhardt* is simply irreconciliable with petitioners' proffered interpretation of the Act, as the American Arbitration Association candidly admits. *See* Br. *Amicus Curiae* at 7-8 n.1.

In *Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, 388 U.S. 395 (1967), this Court held that the Act covered a consulting agreement that "was inextricably tied to [the] interstate transfer and to the continuing operations of an interstate manufacturing and wholesaling business." *Id.* at 401. But this Court was quite careful *not* to expand the FAA to the outer limits of Congress' commerce power. Indeed, it rested its view of the Act on legislative history explaining that the FAA "'reaches not only the actual physical interstate shipment of goods but also contracts relating to interstate commerce.'" *Id.* at 401-02 n.7 (quoting H.R. Rep. No. 96, 68th Cong., 1st Sess. 1 (1924)).

That the FAA extends to an arbitration clause included by two national or regional businesses in a contract that is ancillary to interstate shipments of goods, as in *Prima Paint*, hardly shows that the Act should apply to ordinary consumer contracts involving purely local matters.[11]

Petitioners rely on the statement in *Perry v. Thomas*, 482 U.S. 483 (1987), that the FAA "embodies Congress' intent to provide for the full enforcement of arbitration agreements within the full reach of the Commerce Clause." *Id.* at 490. But this comment was sheer dictum, since the contract at issue there — a broker's employment agreement with Kidder, Peabody — plainly implicated interstate commerce. *See United States Nat'l Bank v. Independent Ins. Agents of Am.*, 113 S. Ct. 2173, 2187 n. 11 (1993) (providing a "valuable reminder about the need to distinguish an opinion's holding from its dicta"). Moreover, since *Perry* this Court has recognized that "[t]he FAA contains no express pre-emptive provision, *nor does it reflect a congressional intent to occupy the entire field of arbitration.*" *Volt Information Sciences*, 489 U.S. at 477 (emphasis added). Of course, if the FAA went to the limits of the Commerce Clause, it would essentially pre-empt the field.

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[11] The majority in *Prima Paint* rejected Justice Black's historical argument, raised in dissent, that the FAA should "apply only to 'contracts between merchants for the interstate shipment of goods.'" *Prima Paint*, 388 U.S. at 401 n.7. The contract in *Prima Paint* was an agreement between a paint manufacturing corporation and another corporation concerning "the facilitation of the purchase of an entire interstate paint business and its re-establishment and operation in another State." *Id.* at 402 n.7. This contract between corporations concerning the movement of an entire business would clearly fall within any understanding of "interstate commerce." Nevertheless, Justice Black's conclusions about the legislative history of the FAA are correct.

II. PETITIONERS' READING OF THE ACT WOULD DEVASTATE CONSUMER INTERESTS

In circumstances involving fully informed parties with equal bargaining power, arbitration may well provide an appropriate method of dispute resolution. But most consumer claims do not arise in such situations. An arbitration clause inserted by the superior party into a form contract, or other in circumstances in which there is a marked imbalance of sophistication, knowledge, and financial resources, functions essentially as an uninformed waiver of the right to trial by jury. Yet the jury is "the single most important institution in the history of Anglo-American law." Judge Morris Arnold, *The Civil Jury in Historical Perspective*, in The American Civil Jury 9-10 (1987).[12]

Waivers of such deep-seated and traditional rights are not lightly inferred, and this Court has made clear that it will "not presume acquiescence in the loss of fundamental rights." *Ohio Bell Tel. Co. v. PUC*, 301 U.S. 292, 307 (1937). Courts therefore must "indulge every reasonable presumption against waiver" of a due process right, *Fuentes v. Shevin*, 407 U.S. 67, 94 n.31 (1972), and such waivers must be knowing and voluntary. *D. H. Overmyer Co. v. Frick Co.*, 405 U.S. 174, 185-86 (1972).

This Court should therefore clarify that the FAA does not encompass consumer contracts. Indeed, this Court has already noted that "categories of contracts otherwise within the Arbitration Act but in which one of the parties characteristically has little bargaining power are expressly excluded [under 9 U.S.C. § 1] from the reach of the Act." *Prima Paint Corp.*, 388 U.S. at 402 n.9 (referring to employment contracts).

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[12] *See also Dimick v. Schimdt*, 293 U.S. 474, 485-86 (1934); *Parkland Hosiery Co. v. Shore*, 439 U.S. 322, 338-44 (1979) (Rehnquist, now C.J., dissenting); Justice Clark, *The American Jury: A Justification*, 1 Valparaiso L. Rev. 1, 1-7 (1966); Judge Higginbotham, *Continuing the Dialogue: Civil Juries and the Allocation of Judicial Power*, 56 Tex. L. Rev. 47, 48-52 (1977).

The resolution of claims by arbitrators rather than the courts radically affects a cause of action. As this Court has recognized, arbitration removes numerous procedural guarantees available to litigants in a court of law as a trade-off for parties seeking an informal resolution of private disputes. *Bernhardt v. Polygraphic Co. of America*, 350 U.S. 198, 203 (1956); *Alexander v. Gardner-Denver Co.*, 415 U.S. 36, 57 (1974). That is why a pre-dispute arbitration agreement between parties of unequal bargaining power has generally been held unenforceable under federal law wherever important rights are involved.[13] Accordingly, arbitration clauses should not be enforced where the potential for misapprehension and unfairness is unacceptably high.[14]

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[13] *See, e.g., U.S. Bulk Carriers v. Arguelles*, 400 U.S. 351, 356 (1971) (seaman's wage claim under 46 U.S.C. § 596 *et seq.* not subject to compulsory arbitration); *Barrentine v. Arkansas-Best Freight System*, 450 U.S. 728, 742-45 (1981) (claim for minimum wages under FLSA nonarbitrable); *Curran v. Merrill Lynch, Pierce, Fenner & Smith*, 622 F.2d 216 (6th Cir. 1980) (claims brought under Commodity Exchange Act nonarbitrable except in certain limited circumstances), *aff'd*, 456 U.S. 353 (1982); *Alexander v. Gardner-Denver Co.*, 415 U.S. 36, 55-59 (1974) (statutory right to trial de novo under Title VII cannot be foreclosed by prior submission of discrimination claim to final arbitration).

[14] For example, in *Bell v. Congress Mortgage Co.*, No. A061946 (Calif. Ct. App. 1st Dist. May 17, 1994), a state appellate court recently refused to enforce an arbitration clause in a mortgage refinancing agreement, explaining that the provision did not "fall within the reasonable expectation of the borrowers." *Id.* The court explained that "the borrowers are generally elderly, unsophisticated and financially distressed individuals who relied upon the good graces of skilled salespersons from a substantial corporate lender." *Id.* "In essence, the adherent surrenders his constitutional right in a trial by jury, as well as virtually all the protections commonly associated with judicial review. . . . [W]e are unwilling to permit the parties to relinquish so casually these fundamental rights." *Id.*; *see also Broemmer v. Abortion Services of Phoenix, Ltd.*, 173 Ariz. 148, 152, 840 P.2d 1013 (Ariz. 1992) (refusing to enforce agreement to arbitrate medical malpractice claims, observing that "there was no conspicuous or explicit waiver of the fundamental right to a jury trial or any evidence that such rights were knowingly, voluntarily and intelligently waived").

The Arbitration Act says nothing to direct a court's inquiry concerning the quality of either party's assent to the arbitration clause other than requiring a written arbitration agreement and referring to grounds for revocation available at common law. But a waiver of the traditional right to jury trial is simply not on a par with other provisions of the "fine print" containing the boilerplate provisions of a contract. Thus, many States have imposed special requirements on the formation of arbitration agreements, in order "to guard against 'surprise' and to insure that consent to arbitration has been knowing and informed." Murray, Processes of Dispute Resolution: The Role of Lawyers 453 (1989). These include requirements that arbitration clauses contain certain language, that they appear in a particular size of type, and that they be separately initialed. *See* Strickland, *The Federal Arbitration Act's Interstate Commerce Requirement: What's Left for State Arbitration Law?*, 21 Hofstra L. Rev. 385, 403 (1992) (listing States). Yet the lower courts have typically ruled, in situations where the FAA governs, that States may not protect consumers in this manner, on the supposed ground that such requirements "discriminate" against arbitration clauses.[15]

Moreover, States have recognized that consumers should be allowed to seek rescission *in court* of contracts that are void for fraud, duress, illegality, or misrepresentation.[16] But, if the FAA were to apply to consumer transactions, those claims could be raised only in arbitration. *Prima Paint*, 388 U.S. at 402-04.

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[15] *See, e.g., Threlkeld & Co. v. Metallgesellshaft, Ltd.*, 923 F.2d 245, 250 (2d Cir.), *cert. dismissed*, 112 S. Ct. 17 (1991); *Securities Indus. Ass'n v. Connolly*, 883 F.2d 1114, 1120 (1st Cir. 1989), *cert. denied*, 495 U.S. 956 (1990); *Webb v. R. Rowland & Co.*, 800 F.2d 803, 806 (8th Cir. 1986). *See also* Br. of American Bankers Ass'n 8-9 & 13 n.2.

[16] *See, e.g., George Engine Co. v. Southern Shipbuilding Corp.*, 350 So.2d 881, 884-86 (La. 1977); *Thayer v. American Fin. Advisors, Inc.*, 322 N.W.2d 599, 602-03 (Minn. 1982); *Fouquette v. First Am. Nat'l Sec., Inc.*, 464 N.W.2d 760, 762-63 (Minn. Ct. App. 1991); *Paramore v. Inter-Regional Fin. Group Leasing Co.*, 316 S.E.2d 90, 92 (1984); Annot., *Claim of Fraud in the Inducement of Contract as Subject to Compulsory Arbitration Clause Contained in Contract*, 11 A.L.R.4th 774 (1982 & 1994 supp.).

Thus, only by declining petitioners' invitation to broaden the scope of the "involving commerce" language can this Court enable States to continue to protect consumers through these important means.

Indeed, to extend the scope of the FAA as petitioners seek would ride roughshod over carefully constructed state policies designed to facilitate arbitration while balancing consumer interests. Many States have adopted special protections in their arbitration statutes to exempt consumer claims altogether.[17] If the pre-emptive effect of the FAA were extended to the limit of Congress' commerce power, these exemptions would be of no practical effect. Surely, Congress did not intend such a far-reaching result.

Given the potential for intrusion into matters of traditional state concern, petitioners' construction of the FAA could not be adopted without a plain statement of congressional intent. *See Gregory v. Ashcroft*, 111 S. Ct. 2395, 2401-03 (1991). This test cannot possibly be met here.

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[17] *See, e.g.*, Ark. Code Ann. § 16-108-201 (excluding "personal injury or tort matters, employer-employee disputes," and claims by "any insured or beneficiary under any insurance policy or annuity contract"); Ga. Code Ann. § 9-9-2(c)(3), (5), (6), (7) & (10) (excluding contracts of insurance, loan agreements and consumer financing agreements involving $25,000.00 or less, contracts for the purchase of consumer goods, contracting involving consumer transactions, and agreements to arbitrate future tort claims arising out of personal injury or wrongful death); Ind. Code Ann. § 34-4-2-1(b) (excluding "all consumer leases, sales, and loan contracts, as . . . defined in the Uniform Consumer Credit Act"); Iowa Code Ann. § 679A1(2)(a) & (b) (excluding contracts of adhesion, contracts between employers and employees, and some tort claims); Kan. Stat. Ann. § 5-401 (excluding contracts of insurance, contracts between employers and employees, and contracts providing for arbitration of tort claims); Mont. Code Ann. § 27-5-114 (excluding, *inter alia*, contracts by individuals for the acquisition of property, services, or credit where the total consideration furnished by the individual is $5,000 or less); S.C. Code Ann. § 15-48-10 (excluding certain claims arising from lawyer-client and doctor-patient relationships, personal injury claims, and claims under any insurance policy or annuity contract).

CONCLUSION

For all these reasons, petitioners' attempt to expand the scope of the Federal Arbitration Act should be rejected. The judgment below should be affirmed.

Respectfully submitted,

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